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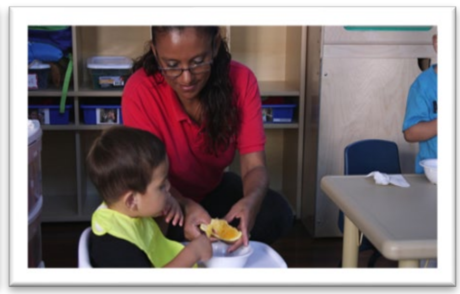
Resources for Family Child Care Businesses



A Series of Articles from Tom Copeland for the National Center on Early Childhood Quality Assurance

Early Childhood National Centers
NATIONAL CENTER ON
Early Childhood Quality Assurance

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I hate answering this question.

Why? Because many family child care providers across the country are not following the proper rules. This can get them into serious trouble.

A person who comes into your home to help you care for children is considered your employee, not an independent contractor. It doesn't matter how little you pay the person or how few hours the person works for you.

There are two exceptions to this general rule. The first situation is a person who is self-employed in the business of providing substitute care for child care providers. Such a person should have a business name registered with your state and their own taxpayer identification number. She should work for more than one child care provider each year and use her own contract.

The second situation is when you hire a substitute through an employment agency and you pay the agency rather than the substitute.

Both of these exceptions are pretty rare. **Anyone else that helps you care for children is your employee.**

You hire someone for 3 hours to watch the children while you go to the dentist – Employee!

You pay a 16-year-old girl in your neighborhood to help you care for school age children for 6 weeks over the summer – Employee!

According to the IRS Child Care Provider Audit Technique Guide: "An employer-employee relationship exists when the business for which the services are performed has the right to direct and control the worker who performs the services." Someone who is helping you care for children is clearly operating under your direction and control.

When I explain this at workshops, no one likes to hear it.

This is because there are many consequences for hiring an employee. You must withhold Social Security/Medicare taxes from the employee's paycheck and pay in these taxes quarterly (or annually, in some cases). You must withhold federal and state income taxes. You must file IRS Forms W-2 and W-3 at the end of the year. You may also have to purchase workers' compensation insurance! (Contact your state for further information.)

Holy Cow! This is a lot of work. But there is no avoiding it. You can get help from a payroll service, or perhaps your tax professional.

The $600 Rule

Don't let a tax preparer or anyone else tell you that you have an independent contractor if you pay someone less than $600 a year.

An independent contractor is someone who works for themselves and does not care for children. This person may clean you house, mow your lawn, or provide an activity for your business (puppet show, swimming lesson, dancing lesson, etc.).

If you pay an independent contract $600 or more, you must issue IRS Form 1099 Misc and give a copy to the independent contractor and the IRS.

But, helpers who work for you caring for children are not independent contractors, so you should not be issuing Form 1099s to them!

Remember, your helpers are employees, not independent contractors, regardless of how little you pay them.

Watch Out!

Unfortunately, providers too often get bad advice about employees from their tax preparer.

If you fail to treat helpers as your employees, the IRS can come after you for back payroll taxes, penalties and interest. Then your state can come after you for failure to pay state unemployment taxes and purchase workers' compensation insurance. The consequences can be severe.

Failure to treat helpers as employees is one of the biggest mistakes I see when I review providers' tax returns.

Start by following the correct rules going forward.

Tom Copeland – www.tomcopelandblog.com

Across the country family child care providers tend to charge less as the children in their care grow older. Preschool rates are lower than toddler rates which are lower than infant rates.

The question is: why?

I posed this question on my Facebook page and received a lot of feedback that was split pretty evenly between providers who lowered their rates as children got older and those who charged the same rate regardless of age.

Why do providers charge less as the children grow older?

- "Babies are harder to care for."
- "Because everyone else in my area does it. I'd love to change to a set weekly rate, but I don't think parents would stick around if I did."
- "Infants require a lot of equipment and more direct attention and are a higher risk."
- "I can only care for two infants and infants are in high demand."

Why do providers charge the same rates regardless of age?

- "I have done this for years but have no idea why!"
- "Every age has their challenges."
- "I feel that a two or three year old is still taking up a spot just like a six month old, so why charge less for older children?"
- "Babies do require extra care, but as a child gets older, she needs more constant interaction. Older children eat more food and tend to break toys more frequently."

There is no right or wrong way to charge for your services. Probably the most important factor driving higher rates for infants is that infant spaces are harder to find and therefore parents will pay more for infant care.

Regardless of how child care providers charge for their services, they tend not to raise their rates much from year to year. This is a shame, considering how hard you work and the additional knowledge and skills you acquire over the years.

Tom Copeland – www.tomcopelandblog.com

Family child care providers can deduct all “ordinary and necessary” expenses for their business. Ordinary and necessary means typical, helpful, appropriate or useful.

Unfortunately, this does not include the costs associated with a dog or cat. In over 35 years of helping providers who were audited by the IRS, I have never won a deduction for dog or cat food. The IRS considers these pets as too personal to be a business deduction.

You may have the children in your care play with your dogs and cats and you may only want to deduct a portion of expenses related to caring for them. No matter. The IRS, in my experience, won’t buy it.

I once helped with an audit where the provider paid to declaw her cat so she wouldn’t harm the children. The auditor would not allow us to deduct this expense.

What pet costs may be deductible?

You could, however, deduct the cost of a dog leash or fence to keep your pet away from the children. Also, you could deduct the cost of pet shots but only if regular pet owners are not required to give their animals these shots.

What about deducting the cost of other pets such as fish, gerbils, birds, or turtles? The answer depends on how you use these pets in your business. If you incorporate them into learning activities with the children, then you could deduct at least a portion of their cost.

For example, you have a fish tank in the children’s playroom and you use the fish to teach children about colors, what fish eat, how fish breathe, etc. Because of these learning activities, you could deduct the cost of the fish, fish tank, food, etc. If your own family enjoys the fish, deduct the Time-Space Percentage of the cost. If your own family does not go into the playroom after day care hours, claim 100% of the cost.

If the fish tank was in your own child’s bedroom and you did not make a point about teaching children about fish, then these costs would not be deductible.

I’ve seen providers who have farm animals such as goats, chickens, ducks, etc. that they incorporated into the curriculum of their program. I advised them to keep records showing what children learned from interacting with these animals (curriculum notes, photos, language in the contract informing parents of these activities, etc.).

Tom Copeland – www.tomcopelandblog.com

Family child care providers are in the caring profession and caring for children is a very personal service.

You probably know more personal information about the families in your care than most of their friends do.

Does this mean the parents in your program are your “friends”? Not in my opinion.

Does your business card say, “Need a Friend?” Does your contract say, “By signing this contract provider agrees to be a friend to the parent”? I don’t think so.

Parents aren’t looking for friends. They are looking for someone to care for their child.

Sometimes, however, parents may appear to want a “friendship” with you. Maybe they want to “hang out” with you, or go out to eat, or they start sharing very personal information that you are uncomfortable listening to.

This can become a problem when the parents try to take advantage of your “friendship” by not paying on time or not following all of your policies.

It can also be a problem if you start treating the parent like a friend and then expect the parent to be your friend. In other words, it can be easy for providers to become personally involved in the lives of the families in their care. You may offer personal advice about their private lives or bend over backwards to assist them in a variety of ways that are not directly related to the care of their child.

There is nothing inherently wrong with this. The problem comes when you expect the parent to treat you like a friend in return. When this doesn’t happen, you are setting yourself up for disappointment and a disruption of your business relationship.

Draw the line

It’s up to you to draw the line between a business relationship and a personal relationship. Nothing prevents you from going shopping with a parent on Saturday or sharing a meal on Sunday. However, for the hours you are caring for the parent’s child, you are running a business.

Sometimes this can be a hard line to draw. Providers don’t want to appear to be unsympathetic, uncaring or even unfriendly. But, there is a difference between being friendly and being friends.

Here are some tips about drawing this line:

- Clearly set your rules when parents first enroll
- Enforce your rules consistently, particularly about payments and pick up times
- Limit the opportunities for small talk at pickup times by having other things to do

- Politely ignore or rebuff friendship attempts. One provider recommended saying, “I’m so flattered, but I’ve found it best not to mix business and pleasure. Have a great weekend.” Or “I already have plans.”

If you haven’t been doing these things, you can start now.

Tom Copeland – www.tomcopelandblog.com

Are You In Line For a Bonus This Year?

Some parents in your family child care program may be able to give you more money without it costing them anything.

How is this possible?

Many employers offer a payroll option that allows their employees to set aside some of their wages to pay for child care expenses, without the money being taxed.

These plans are called dependent care plans, flexible spending account, cafeteria plans, salary reductions plans, or pre-tax spending accounts.

Parents who participate in these plans can save hundreds of dollars in taxes by setting aside a maximum of $5,000 per year, per family. Parents decide how much money to set aside before the year begins and their employer keeps any unspent money.

You want to make sure that you, not the employer, receive any unspent money.

Here's how. Calculate how much parents will pay your program by the end of this year. If the amount is more than $5,000, there is no unspent money and there is nothing further you can do.

If the amount is less than $5,000, then say this to the parent:

"I know that you participate in a dependent care plan at work. My records indicate that you will pay me approximately $X by the end of the year. If you set aside more money in your plan than this amount, this unspent money will be kept by your employer. However, if you give me this unspent money, I will use it to increase the quality of care for your child."

For example, if the parent will pay you $4,800 this year and she set aside $5,000, you want the parent to give you the extra $200.

Some parents may want you to apply the unspent money to care that you deliver the next year. This is illegal, so do not agree to this. Money set aside under these plans can only be spent on child care services delivered this year.

If the parent agrees to give you the money, just add the extra amount to the next parent payment. If there is $200 in unspent money, and you regularly charge $180 a week, ask the parent to pay you $380 for care next week.

If you want, you can submit a bill to a parent in January or February next year for the unspent money from this year, as long as you indicate on the bill that the payment is for child care services this year.

(Parents have until next March 31st to submit a receipt to their employer for child care services delivered this year.)

There is nothing wrong with adding an extra amount onto your normal child care bill, or giving the parent another receipt for the same week in December.

The parent should submit a receipt to their employer for this money exactly the same way they submit all other payment receipts. Because this money is being spent on child care services it should not be identified as a bonus or charitable contribution. There is nothing wrong with the parent deciding to pay you an extra amount for the care you provide.

Since the parents will lose this money unless they give it to you, most parents will agree to this arrangement. You must report any extra money you receive as income, and you can deduct any items you purchase for your business with this money. I have heard from many providers who have received extra money from parents, ranging from $50 to $1,500.

Don't be shy about asking parents for any unspent money! Tell them you will use the money to improve the quality of your program.

Under what situations would a parent not spend all the money set aside in their plan? Parents who changed caregivers in the middle of the year, parents who missed a lot of work because of illness, parents who overestimated their child care expenses, etc.

Note: A change in the law a few years ago allows employers to extend the time employees may use their money set aside in these plans for child care services through March 15th of the following year. In other words, if a parent has $200 in unspent money as of December 31st, they might be able to use it for child care delivered January 1st – March 15th.

It's up to the employer to adopt this rule in their dependent care plan. If this is the case, it's much more unlikely that employees will have unspent money to give you.

What have you got to lose by asking parents if they have used up all the money in their dependent care plans?

Tom Copeland – www.tomcopelandblog.com

Are You Liable When a Child is Injured in Your Care?

A family child care provider once wrote me:

“A five year old boy came to my home from preschool and brought in pea gravel from the school playground. He and a four year old girl were playing and he convinced her to put a pebble in her ear. She came to me crying. When I couldn’t get it out, I called her mother.

They went to the emergency room and the on-call doctor pushed it in further in the process of trying to get it out. They went to a specialist the next day and the child ended up needing surgery to remove it.”

The family had a high deductible medical insurance policy. They don’t want to pay the large medical bill and asked me to pay some of the cost.

Am I liable?”

The short answer is yes. In general, since you are the responsible adult while children are in your care, you are liable for any injury suffered by a child.

Your homeowners insurance policy is unlikely to cover you in this situation. If you have business liability insurance, you will probably be covered for medical expenses up to around $10,000.

If you don’t have business liability insurance, you should tell the parent you don’t have insurance. This may discourage them from trying to sue you. You could offer to pay some of the medical bill in the hope that this will end the matter. However, if the child later suffers complications, the parents could decide to sue you later. If they do, you are likely to lose.

With more and more families forced to purchase health insurance policies with high deductibles, this scenario is likely to occur more often. Your only protection is to purchase adequate business liability insurance.

Whenever there is an injury to a child in your program, take the following steps:

1. Report it immediately to your child care licensor
2. Report it immediately to your business liability insurance agent
3. Keep a careful written log of all events surrounding the incident

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Calculating your Time-Space Percentage correctly will have the biggest impact on reducing your taxes.

Many family child care providers, and some tax preparers, fail to take advantage of this unique IRS rule and, as a result, pay too much in taxes. Your Time-Space Percentage is entered onto IRS Form 8829 Expenses for Business Use of Your Home.

The Time-Space Percentage is made up of a Time Percent and a Space Percent.

The Time Percent is based on the number of hours you use your home for business activities, including the hours children are present as well as the hours you conduct business activities when children are not present.

The Space Percent is based on the number of rooms you use either on a regular basis for your business or exclusively for your business.

I've created an Excel Spreadsheet that you can use to calculate your Time-Space Percentage:

http://tomcopelandblog.com/wp-content/uploads/2020/05/Time-Space-final-3.xlsx

Here are the numbers you need to complete this spreadsheet:

- Total number of square feet in your home
- Number of square feet used exclusively for your business (if you have exclusive use rooms)
- Number of square feet used regularly for your business
- Number of hours you cared for children in your home
- Number of hours you did business activities in your home when children were not present
- If you were not in business for the full year, the number of hours there were in the year when you were in business.

Here's the instructions on how to fill out this spreadsheet:

Line 3: Enter the total number of square feet in your home. Include the square feet of a garage, basement and deck. Don't count outdoor space such as a lawn area, patio or driveway. This number should appear on IRS Form 8829, line 2.

Line 4: Enter the total number of square feet used regularly for your business. Regular use means you use it two-three times per week for some business activity. Children do not have to be in a room for it to be counted as regular use. Such rooms might include storage rooms, office, laundry room, furnace area, etc. If children sleep on your bed several times a week, that's regular use. If children don't enter your bedroom but you have a desk, computer and a file cabinet that you use on a regular basis, count your bedroom as regular use. If you don't have any exclusive use rooms, this number should appear on IRS Form 8829, line 1.

Line 5: This represents your Space Percent if you only have regular use rooms and no exclusive use rooms. It's calculated by dividing the regular square feet by the total square feet in your home.

Line 7: Enter the number of hours you spend caring for children in your home for the year from the moment the first child arrived until the last child leaves. If your pickup time is 6pm but the last parent doesn't walk out until 6:30, count the extra half hour. If children stay overnight, count all this time. So, if you cared for children from 6am to 5pm five days a week, 50 weeks a year, your total would be 2,750 hours (11 hours a day x 5 days a week x 50 weeks = 2,750 hours).

Line 8: Enter the number of hours you spend in your home on business activities when children are not present. This can include: cleaning, activity preparation, meal preparation, talking to parents on the phone, parent interviews, time on the Internet, time reading my blog posts!, etc. Ideally, you should carefully tracking these hours for two months each year and use the average for those two months. If you use the KidKare software program, see my instructional video on how to track these hours: https://www.facebook.com/watch/?v=1795935210469601

Line 9: This line automatically adds up all the hours you spent in your home on business activities. This number should appear on Form 8829, line 4.

Line 10: There are 8,760 hours in the year. If you were in business for twelve months, enter this number. If you started your business after January 1st or ended your business before December 31st, enter the number of hours there were for the months you were in business. This number should appear on Form 8829, line 5.

Line 11: This line automatically calculates your Time percent. This number should appear on IRS Form 8829, line 6.

Line 13: This line automatically calculates your Time-Space% when you have no exclusive use rooms.

Line 15: Enter the total number of square feet you use exclusively for your business. An exclusive use room is a room that is never, ever used personally. This is a strict rule. What if you have a basement area that is used exclusively for your business, but there is also a furnace, water heater or laundry room in the same area? Draw a line around the rooms that are regularly, but not exclusively, used for your business and count those areas a regular use and count the remaining space as exclusively used. If you have an exclusive use rule, IRS Form 8829 has special instructions on how to fill out this form (See page 2).

Line 16: This line automatically calculates your Time-Space% if you do have exclusive use rooms.

If you use a tax preparer or use any online tax software programs (TurboTax, H&R Block, TaxAct), check to see that the number that appears on your Form 8829, line 7 is the same as the number on lines 15 or 16 of this spreadsheet. If not, ask your tax preparer why there is a difference or review what you entered into the software program.

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Can I Deduct an Unpaid Child Care Bill?

Unfortunately not.

I know from my travels around the country that many family child care providers do not receive all the money that is owed them. This problem is more severe during financial hard times.

Here are some situations where this occurs:

- A parent bounces a check or leaves owing money for child care provided.
- A parent leaves without giving proper notice under the contract and doesn't pay for the last two weeks of care.
- A child care subsidy program declares that a parent is no longer eligible and tells the child care provider she will not be paid.

In all of these situations, there is an unpaid child care bill and the child care provider is owed money. Unless she pressures the parent to pay, or takes the parent to court, she will have less income at the end of the year. How should this be treated on her tax return?

You must report all money you received caring for children on IRS Form Schedule C. If you didn't receive money you earned, you do not report it as income. However, money you earned but didn't receive cannot be reported as a business expense. If the parent owes you money in 2021 and you collect it in 2022, report it as income in 2022.

Similarly, you cannot deduct a discount (or a scholarship) you give to a parent.

Because you will be reporting less income, your taxes will be lower. I realize that this is small consolation.

The only way to be sure you are not owed money is to require parents to pay in advance. When caring for subsidized families, you may or may not be able to require parents to pay in advance. Check with your subsidy worker.

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When you use your vehicle in your family child care business, you can deduct a portion of the cost of operating it. Because the deductions for vehicle expenses can help significantly reduce your taxes, you want to be sure you are claiming them properly.

There are two ways to claim vehicle expenses: the Standard Mileage Method or the Actual Expenses Method.

The Actual Expenses Method

Using this method allows you to deduct the business portion of all the actual expenses of operating your vehicle. These include:

Gas, oil changes, repairs, car insurance, tires, emergency road service, ice scraper, jumper cables, tune-up, car wash/wax, windshield wiper fluid, as well as parking/tolls/ferry, car loan interest, car property tax and so on.

You must save your receipts for all these purchases.

You can also claim depreciation on the vehicle based on its fair market value at the time you first used it in your business.

The business portion is determined by dividing the number of business miles you drove in the year by the total number of miles you drove. For example, 2,000 business miles divided by 10,000 total miles = 20% business. Add up all your actual vehicle expenses (except depreciation) and multiply by your business percentage to claim your deduction. Depreciation is calculated separately.

Which method is better?

Most child care providers use the standard mileage method to claim vehicle expenses because it’s easier to keep records. However, many would be better off using the actual expenses method.

In the first year you use your vehicle for your business, you can choose either method. However, if you choose the Actual Expenses Method you must continue using this method for as long as you use that vehicle in your business. If you choose the Standard Mileage Method in the first year, you can switch to the actual method in later years. If you use more than one vehicle for your business, you can choose one method for one vehicle and another method for the other.

Leasing

If you lease a vehicle ,you can choose either method when deducting expenses. If you choose the actual method, you can deduct the business portion of the lease, gas, insurance, oil changes, and other out-of-pocket expenses.

In general, leasing will cost you more money over the long run than buying the vehicle.

Vehicle expenses can be a major business deduction for family childcare providers – and are often audited by the IRS. Therefore, it pays to know what you can deduct and how to keep accurate records.

You can count a trip as a business trip if the "primary" purpose of the trip is business. Primary purpose means that more than 50% of the reason for the trip is business. This includes children's field trips, trips to the bank to deposit parent fees, and trips to trainings. A trip to the grocery could be claimed as a business trip if more than 50% of the food purchased was for the business.

You must have an "adequate record" to show that you made a business trip: calendar notations, receipts, cancelled checks, credit or debit card statements, field trip permission forms, training certificates, mileage log, photographs, and other written records. You may want to review these records monthly to make sure you've identified all your business trips.

You are not required to keep a mileage log of odometer readings. You do want to record the odometer reading of your vehicle at the beginning and end of each year.

There are two ways to claim vehicle expenses: the standard mileage method or the actual expenses method.

Standard Mileage Method

If you use the standard mileage method, you can claim the following expenses for your vehicle:

1. Business mileage rate
    a. The business mileage rate for 2022 is $.58.5 per mile.
2. Parking/toll/ferry expenses
3. The business portion of car loan interest and personal property tax

Personal property tax is a tax paid at the time you renew your vehicle registration. It's not the tax you pay when buying a vehicle. Look on your annual vehicle registration bill to see if there is a tax. You can only deduct the tax, not the registration fee. Not all states have a personal property tax.

To determine the business portion, divide the number of business miles you drove in the year by the total number of miles you drove. For example, 2,000 business miles divided by 10,000 total miles = 20% business. If your car loan interest was $500 for the year, you could deduct $100 ($500 x 20%).

You cannot deduct any other vehicle expenses when using the standard mileage method. This includes car insurance, gas, oil, repairs, and so on. The standard mileage rate is designed to cover these expenses.

Tom Copeland – www.tomcopelandblog.com

There will come a day when you close down your business.

When that day comes, here are some tax and non-tax issues to consider:

Tax Issues

Claim all your business income and expenses for the last year you were in business.

When you calculate your Time-Space % for your final year, adjust the number of hours in the year on IRS Form 8829 Expenses for Business Use of Your Home if you closed down before the end of the year. You can only claim house expenses for the months you were in business.

If you have been depreciating items used in your business, you normally will only get a half year's worth of depreciation in the year you go out of business, no matter what month you close down.

The exception is for depreciation on your home and home improvements. For these items, you claim the last year of depreciation based on the month you close down.

If before you go out of business you replace items you have been depreciating (carpet, vinyl or wood floors, furniture, appliances, etc.), you will be entitled to deduct all of the remaining unclaimed depreciation on these items on your last business tax forms.

For example, if you replace the carpeting in your playroom before you go out of business, and it's in the fourth year of depreciation, you can deduct the fourth-seventh years of depreciation. If you wait until after you go out of business to replace such items, you will not be able to deduct any of the remaining unclaimed depreciation.

After going out of business, the only thing you need to remember about taxes is that you will owe some taxes when you sell your home. Whether you sell your home immediately after going out of business, or years later, you will owe taxes on the depreciation you claimed on your home since May, 1997.

You will owe this tax whether or not you actually claimed depreciation on your home. Therefore, when you do start to make plans to sell your home, contact a tax professional to help you deal with the tax consequences of this action.

You don't have to announce to the IRS (or your state Department of Revenue) that you are going out of business. You simply don't file any of the business tax forms (Form 8829, Schedule C, Form 4562, etc.) in the year after you go out of business.

Non-Tax Issues

Contact your child care licensor, your local Child Care Resource and Referral agency and your family child care association so they can update their records.

Contact your insurance agent for your home and car. You may be entitled to a reduced insurance rate depending on your circumstances.

Contact your business liability insurance agent. You may get a refund for cancelling your insurance policy before the end of the year. Save a copy of your insurance policy until the youngest child in your program (at the time you closed your business) reaches age 21. Before then, it may be possible for a child to sue you for an injury that occurred while in your care.

Notify your parents, in writing, that you are closing your business. Keep copies of this notice for your records. If your contract requires you to give parents a two-week notice, do so.

But, if you tell parents months in advance that you are closing your business, some parents may want to terminate earlier. Take this into consideration when deciding when to inform parents of your decision.

If you are closing down your business, I hope you take a moment to appreciate how all of your hard work over the years has had a positive impact on so many children. Congratulations!

Tom Copeland – www.tomcopelandblog.com

For most family childcare providers, the answer is “Both!”

Family childcare providers love children. It’s their number one motivating factor. But earning money is also important.

Unfortunately, in our society we undervalue the work of providers. Federal and state governments drastically under-fund the childcare system. Many parents can’t afford the true cost of childcare. As a result, providers are often forced to subsidize the system with low wages.

Yet some parents assume providers should be happy to do their work without regard for money.

This comes up when a parent complains about paying a late pickup fee, leaves without giving a two-week notice, or objects to a provider enforcing her contract or policies. If a provider tries to enforce her rules, the parent sometimes acts offended, and might say, “You’re just in it for the money.”

This attitude is an attempt to shame providers into not enforcing their rules. But it’s also a reflection of how society views caregivers of young children as less worthy citizens. It’s like saying, “You don’t deserve to be paid for your work.”

It’s also a statement about the undervaluing of work primarily done by women.

The irony is that parents who think, “This provider only cares about money” don’t realize that providers as a group don’t make a lot of money! In fact, most parents probably make more money than most providers!

So, how should you respond to parents who complain about your fees? First, for parents who want high quality care, the cost of childcare can be a real barrier. Childcare is expensive for many. But the same can be said for the cost of college, a mortgage, and many other items. So, you can acknowledge this fact.

Second, don’t apologize for the rates you charge. Not all parents can afford you. Unless your goal is to serve only low-income families, it’s okay to run your business so that not everyone can afford it.

Third, if providing childcare is a career for you, you want to be in business for many years and support your own family financially. If you don’t charge a reasonable fee, it’s less likely you will be able to accomplish this goal.

Running a successful business while loving the children in your care is not a contradiction. You can do both.

The problem of the high cost of childcare can’t be solved by providers lowering their rates, or parents paying a lot more than they currently do. Although some parents can pay a lot more!

Ultimately, there needs to be more government support for both parents and providers to make high quality care more affordable and accessible, while offering a living wage to providers.

Tom Copeland – www.tomcopelandblog.com

I was reviewing a family child care provider's tax return today and asked her where the number for her supply expenses came from.

She didn't know. She used a tax preparer, gave him her receipts and assumed he put the correct numbers on her tax return.

But, she didn't know if the numbers were correct.

I see this all the time.

Family child care providers are responsible for the numbers that appear on their tax return.

If you don't know where a number comes from and you can't back it up with a receipt or other record, you will be in trouble if you are ever audited.

This is true even if your tax preparer made a mistake in putting down the wrong number!

Here's what I see when I'm helping providers who are audited, or when I'm reviewing their tax forms:

A provider's Schedule C says, "Supplies $1,200." I ask the provider, "Where did this number come from?" The provider answers, "I don't know. My tax preparer entered it."

I ask, "Does this represent supplies that were all 100% business, all shared, or some of both?" Answer, "I don't know."

Or, I'll ask, "Was your Food Program income reported as income on your Schedule C?" or "What rooms were not counted as regularly used for your business?"

The provider doesn't know the answer.

The problem here is not knowing what's on your tax return. Maybe the numbers are correct, but maybe they aren't. You need to know.

Therefore, before signing your tax return, review each line on your Schedule C, Form 8829 and Form 4562 to make sure your records back up these numbers. If not, ask your tax preparer where the number on the tax forms came from.

Sometimes providers list their business expenses under expense categories that don't match the expense categories that their tax preparer uses. Although, in the end, it doesn't matter what expense category you choose for each expense, you need to be able to match your expenses to specific lines on your tax return.

The primary problem

The primary problem I see is that providers and/or tax preparers are not making a distinction between items that are 100% business and those items that are used for both business and personal purposes.

If a tax preparer asks, “What did you spend on supplies?”, this is the wrong question! The correct questions are, “How much did you spend on supplies used 100% for your business?” and “How much did you spend on supplies that were used for both business and personal purposes? ”These same questions should be asked for almost all expense categories.

My Family Child Care Tax Companion is a tool providers can use to avoid this problem. If you fill out the worksheets in the book, it will ask you about 100% items versus shared items. You then can give the book to your tax preparer so they have the correct information to fill out your tax return.

After you get the book back, you can compare what you entered to what is on your tax return. Then you can ask questions if the numbers don’t match. It’s the responsibility of a tax preparer to answer your questions about what they put on your tax return. Don’t file your taxes until you are satisfied you can defend each line in an audit.

The KidKare software makes it easier to track where the numbers on your tax return come from. You can print out several end-of-year reports that mirror the Schedule C and Form 8829 tax forms. If you are doing your own taxes, you can easily transfer your numbers from these reports onto your tax forms.

If you use a tax preparer, you can easily monitor if the numbers on your tax forms are supported by your KidKare reports.

Tom Copeland – www.tomcopelandblog.com

What should you charge for caring for children?

Child care rates vary widely primarily by geographic area. The more affluent neighborhood you live in, the more you can charge.

However, within your neighborhood your rates should match the quality of the care you offer.

Unfortunately, many family child care providers make the mistake of setting their rates according to the “average” rate in their community.

The problem with an “average” rate is that there are many providers charging a lot more and many charging a lot less. There is usually a wide gap between the lowest and highest rate for every age group in family child care.

Therefore, your rates should only be “average” if the quality of your care is average.

If your quality is “high”, your rates should be in the top 20th percentile of rates in your area.

Some providers keep their rates low to help out low-income parents. This is admirable. Other providers only care for subsidized children, so they have no control over what they can earn.

If you want to make more money

If you want to make more money, it’s important to be able to identify the benefits of your program and communicate them to parents.

The more benefits you offer parents, the easier it will be to charge more for your services.

Some providers will say, “If I charge more, parents will leave (or new parents won’t enroll) and go to another provider who charges less.” That may happen. However, there are always providers charging less (and more!) than you. If you are trying to compete on the basis of your price, you are probably short-changing yourself unless you are offering low quality care.

Are you a low quality, “average” provider? I don’t think so!

Even a small rate increase can make a big difference in your income. If you are charging $170 a week and increase your rates by 3%, that represents $5.10 more per week per child. If you work 52 weeks a year, the difference that year will add up to $265.20 ($5.10 x 52 weeks) per child.

If there are five children in your program, you will earn $1,326 more that year. If you raise your rates by another 3% the next year, you will earn another $1,365. At the end of two years you will have earned an additional $2,691.

If your current rates do not reflect the quality of care your offer, set a goal to move closer in the near future.

Tom Copeland – www.tomcopelandblog.com

Does Your Homeowners Insurance Still Cover You?

The surprising answer for many family child care providers is “probably not.” Homeowners insurance is personal insurance and is not meant to cover risks associated with any business, including caring for children.

Homeowners insurance covers three basic things:

1. Your house and other structures on your property (garage)
2. The contents of your home, and
3. Some personal liability protection.

When you start using your home for your family child care business, you may lose some of the insurance protection you once had. This can come as a shock when you make a claim against your homeowners insurance policy and find out that the claim is not covered!

Your home

Some homeowners insurance policies say “no coverage for any claiming arising out of or in connection with a business.” If your policy says this and your house is damaged in a hurricane you may get nothing! If your policy says, “family child care covered up to four children” and you have five children in care and a fire damages your kitchen, you may get nothing! Although such policies are rare, they do exist. A provider in Minnesota once had hail damage on her roof. When the insurance company found out she did child care, they stopped the contractors from finishing the repairs.

The contents of your home

Homeowners insurance policies insure the contents of your home to the tune of hundreds of thousands of dollars. This covers damage or destruction of your furniture, appliance, clothing, and everything you brought into your home. However, most policies only cover “business property” up to $2,000.

The key question is what the policy means by “business property.” In one case, a provider’s home was entirely destroyed in a tornado. Her policy only paid out $2,000 for all the contents of her home because they said property that is ever used in a business is considered “business property” subject to the $2,000 limit. Because almost everything in your home is used for your business (washer, dryer, tables, chairs, television, rugs, etc.), you need to know the extent of your coverage.

What to do?

You must contact your homeowners insurance agent and tell him/her you are a family child care provider caring for ___ number of children. Ask if your home and its contents care covered under your policy. If your agent says you are covered, ask for her to send you a letter stating this. Unless you have something in writing, you should assume your policy does not fully cover you.

I've talked to a number of providers over the years who were told by their insurance agent that they were covered, only to find out later that the insurance company would not cover them. This is why it is critical to get in writing stating something to the effect that "the insurance company is aware of the child care business in your home and this has no adverse effect on the level of your protection under your homeowners policy."

If your homeowners policy does not cover your business at all, you will need to purchase a commercial insurance policy (or shop around for another insurance company). If your policy does not cover your contents you need to purchase a business property insurance policy. Your homeowners agent should be able to get this insurance for you. The cost will not be large. Some business liability insurance policies may offer some business property insurance coverage, but it's unlikely it will adequately cover all of your business property.

Personal liability protection

Your homeowners insurance policy will not pay claims or defend you if a child or parent in your program is injured. You need business liability insurance to cover you for the liability risks of operating your child care business; primarily for bodily injury claims and lawsuits.

Tom Copeland – www.tomcopelandblog.com

Does Your Vehicle Insurance Still Cover You?

Probably the biggest financial risk a family child care provider can take is to get into a vehicle with children.

You run the risk of multiple injuries, property damage and lawsuits.

A family child care provider in Minnesota was transporting four children in her van when it caught fire on the freeway. Two children died. Because she didn't have adequate vehicle insurance she is out of business and has hundreds of thousands of dollars of claims against her that she cannot pay.

Your homeowners and business liability insurance policies will not protect you when you are in your vehicle.

If you use your car only "occasionally" for your business you may not need more car insurance than you currently have. If you use your car "regularly" for your business you may need commercial car insurance.

It's imperative that you find out whether your current vehicle insurance policy covers you. This means contacting your vehicle insurance agent and describing in detail how you use your vehicle in your business: Do you transport children daily, weekly, monthly, rarely, never? Do you go to the bank, training workshops, grocery stores, hardware stores, etc.?

After describing all the ways you use your car for your business, ask the question, "Am I covered in all of these situations?"

If your insurance agent says your current policy covers you, ask them to put it in writing. If you don't have it in writing, it's likely you are not covered.

How much coverage?

You want bodily injury and property damage coverage of at least $500,000 for each accident. You can also purchase limits of $250,000 Bodily Injury for each person/$500,000 Bodily Injury for each Occurrence and $250,000 Property Damage.

You want uninsured motorist bodily injury coverage of at least $500,000 for each person and each accident. Or split the limits as shown above.

You want under-insured motorist bodily injury coverage of at least $500,000 for each person and each accident. Or split the limits as shown above.

You want a higher deductible ($1,000) to help reduce the cost of the insurance policy.

Umbrella insurance

Some providers purchase an umbrella insurance policy that raises the coverage limits on their homeowners and car insurance policies. Before purchasing an umbrella policy, find out if this will increase the coverage when there is an accident during a business trip.

Transport children?

If you regularly transport children, you may find that you must purchase commercial vehicle insurance to be adequately covered. The cost of such insurance can vary a lot. Some family child care providers have concluded that they can't afford the insurance and stop transporting children.

You may find it is cheaper to use public transportation or hire a van when transporting children.

Summary

Most providers have not contacted their insurance agent to see if their vehicle insurance covers them when they use their vehicle for their business. Some insurance companies will not cover child care providers, so you need to discuss this with your insurance agent.

Conclusion: Do not get into a vehicle unless you are adequately insured and have it in writing!

Tom Copeland – www.tomcopelandblog.com

"A parent left my program owing me money. What can I do?"

I've been getting this question at least once a week from family child care providers for the last 30+ years.

There are two rules you can adopt in your contract that will ensure that parents will never again leave your program owing you money:

1. Parent will pay at least one week in advance.
2. Parent will pay in advance for the last two weeks of care.

If you enforce these two rules you will never have to sue a parent for an unpaid bill. These rules are reasonable and affordable. If a parent can't to afford to pay either of these amounts in advance, ask them to pay a little extra each week over time.

If the parent receives a state subsidy and pays you a co-payment, ask for the co-payment in advance.

Being paid in advance gives you more control if you decide to end the relationship. If you want to end your contract early, simply give the parent back the payment for the last two weeks.

Requiring advance payment can give you more confidence, financial security and peace of mind. You may be reluctant to enforce your rules if you are afraid that your clients will leave owing you money. Without this fear, you can be more assertive about enforcing your rules – and as a result you'll probably have fewer conflicts.

Over the years I've seen more and more child care providers institute these two rules without incident. It's the right thing to do.

Tom Copeland – www.tomcopelandblog.com

Establish a Vehicle Replacement Fund for the New Year

My father always told me that the only things in life I should borrow money for were a home, a home improvement, and my education. Everything else should be paid for with cash.

“If you can’t afford to pay with cash, you can’t afford it,” he told me.

I think this is good advice for everyone, including family child care providers.

This means that child care providers should pay cash for their vehicles.

Of course this is difficult for many to do. Most child care providers, like everyone else, put some money down and take out a loan to buy a vehicle. As a result, you pay interest on your loan. Money you spend on interest could instead be used to meet other short or long-term financial goals.

Here’s a plan for how to establish a vehicle replacement fund that will allow you to pay cash for your vehicle.

Step One: Hold onto your current vehicle for as long as you can and pay off any debt on it as soon as possible.

Step Two: Start putting aside money into a savings account each month for your next vehicle.

Step Three: When you have to buy a new vehicle, make as big a down payment as you can using the money you have been setting aside and other money you may have at the time.

Step Four: Pay off the new vehicle loan as fast as possible and continue setting aside money for your next vehicle.

Hopefully, each time you buy a vehicle your down payment will be substantially greater until you are able to pay the full amount in cash. This may take you a number of years before you can meet this goal. But it’s worth it!

We live in a vehicle-obsessed society that urges us to borrow money to buy fancy new vehicles every few years. Paying cash for a vehicle is a better way to manage your money and keep more for yourself.

Tom Copeland – www.tomcopelandblog.com

If you are considering establishing a new family child care business (or you have already started the process), here is a checklist of business issues you should address before caring for children:

Regulatory Issues

Contact your local child care licensor to find out if there are any serious barriers to meeting state licensing requirements. These could include:

- Safety standards: Requirements that you make safety modifications to your home, such as installing an egress window in the basement or adding a fence. Your home may also have to pass inspections by the building and fire departments.
- Space standards: Requirements that you have enough indoor and outdoor square footage available for the number of children you wish to care for.
- Disqualification factors: Requirements that you have a criminal background check that may include looking at any history of mental illness or chemical dependency for you or other family members.

Legal Issues

Check with your appropriate local agency to insure that none of the following legal barriers apply to your business:

- Zoning laws: City or county zoning ordinances may limit your ability to run a business out of your home.
- Deed restrictions: Private landowners, such as homeowners' associations, home developers, or landlords may have restrictions in their deeds that limit your ability to operate your business. Read all deeds and covenants for your property before opening your business.
- Business name: Although you are not required to adopt a separate name for your business, if you do some states require that you register your business name with your state secretary of state's office.
- Business structure: The vast majority of family child care providers operate their business as a sole proprietorship (also known as self-employed). There is no paperwork to file before you start caring for children. If you do consider operating as a partnership, corporation, or limited liability company (LLC), I strongly recommend that you consult with an attorney and tax professional for advice before you make this decision. There are many drawbacks to operating other than a sole proprietorship. For a detailed description of what business structure to choose, see my Family Child Care Legal & Insurance Guide (https://www.redleafpress.org/Family-Child-Care-Legal-and-Insurance-Guide-P65.aspx).
- Business location: If you are considering running your business out of a building that you do not live in, consult first with your child care licensor, Food Program sponsor, and zoning office to find out if this can be done in your area.

If you have an opening in your family child care program, offering a finder's fee is the first thing you should consider offering the parents in your program.

It's a marketing tactic that has helped many child care providers fill openings in their program.

What's a finder's fee?

A finder's fee is a gift you give to parents in your program who have referred new families to you. Tell your parents, "If you refer a new family to my program and I enroll the family, I will give you a finder's fee after the new parent has paid me for at least a month of child care."

The finder's fee you offer parents in your program can be money, gift cards, free child care or anything else you want. The amount of finder's fees I've seen from talking with child care providers across the country ranges from $25-$50 in most cases, or free care from a day to a week.

If you give out cash or a gift card, you can deduct 100% of the cost as an advertising expense.

This is a no-lose way to promote your program. Unlike paid advertising, you will only pay something after you've enrolled a new family and received at least a month's worth of child care. The parents in your program will be initially spreading good worth of mouth without cost to you. They will also be selective in who they refer to you because they will want the new child to be compatible with their own child.

When I discuss offering a finder's fee in my workshops, I find that few child care providers are willing to pay more than $50. When you think about how many thousands of dollars a new client is worth to you over the years they remain in your program, I think a finder's fee as high as several hundred dollars is well worth it!

In fact, during financial hard times a high finder's fee may encourage current families who may be financially struggling to make more of an effort to give your referrals.

Some child care providers object to offering a finder's fee because they believe doing so makes them look desperate or lowers the value of their services. Instead, they give parents a thank-you note. I don't share this view. Other businesses offer deals to customers, and few complain.

You could also consider offering a finder's fee to clients who have left your program, other child care providers, or parents who have contacted you but decided not to enroll their child in your program!

Tom Copeland – www.tomcopelandblog.com

Four Key Ingredients of an Effective Contract

Here are the four key ingredients of an effective contract that will help family child care providers communicate clearly and reduce potential conflicts with parents:

1. Make your contract work for you. You can set whatever rules you want for your program. You can run a highly structured or unstructured program. You can use any curriculum you want or design your own. You are the boss of your own program. The only exception to this is that you cannot discriminate based on race, sex, religion, national origin, or disability. Your state may have additional rules against discrimination.
2. Create two separate documents: a contract and policies. Your contract is a legal document that spells out the hours and days you will provide care in exchange for money paid by the parent. Any change to a written contract must be in writing and signed by both parties. Your policies contain all the rules for how your program will operate (sick policy, meal policy, activities, behavior guidance, etc.). You can change your policies at will.
3. Adopt these two rules:
    a. Client will pay at least one week in advance
    b. Client will pay in advance for the last two weeks of care

    If you enforce these two rules, you will never have a parent leave your program owing you money. These two rules are reasonable and affordable; if the parent can't pay this full amount in advance, you can allow parents to pay a little extra each week over time. For parents who receive state financial assistance, you may or may not be able to adopt these rules.

4. Enforce your rules with a consequence. Do not be hesitant to enforce your rules if a parent violates them. The way to enforce your rules is to give parents a consequence for not following them. If a parent is late, charge a late fee. If a parent refuses to pay you on time, give the parent a fair warning, then terminate if her behavior doesn't change. Parents who are given clear rules to follow and understand the consequences of not following them are less likely to cause problems.

Tom Copeland – www.tomcopelandblog.com

The best part of being a family child care provider is caring for children.

Probably the worst part is taking care of the business side of what you do.

For new child care providers and for those who are getting ready to open, there are many business issues that should be addressed as soon as possible. (And, if you are an experienced provider who hasn't dealt with these issues before, it's never too late!)

Here's a checklist of the key business issues you should address:

Organizations

- Contact your local child care licensing agency and meet all state child care laws.
- Join the Child and Adult Care Food Program (https://www.fns.usda.gov/contacts/contact-map) to receive about $600 to $1,250 per child per year for serving nutritious food.
- Contact your local Child Care Resource and Referral Agency (https://www.childcareaware.org/resources/ccrr-search/#section=searchbyzip) and take advantage of their many services (training, marketing, support).
- Join your local, state and National Family Child Care Association (www.nafcc.org) and receive a series of benefits (networking, advocacy, training, and more).

Record Keeping/Taxes

- Save receipts for all expenses associated with your house (cleaning supplies, toilet paper, light bulbs, welcome mat, dishwasher detergent, etc.)
- Keep records of all meals and snacks served to the children in your care. By using the standard meal allowance method of claiming food expenses, you can deduct about $1,140 a year per child.
- Track all the hours you use your home for your business, particularly those hours when you are doing business activities when children are not in your home.
- Purchase the KidKare (www.kidkare.com) software program to help you track income, submit Food Program claims, record expenses, and much more.

Contracts/Policies

- Create a written contract and policies for parents that establish the rules you want to make and enforce these rules consistently.
- Include these two rules in your contract: 1) Parents must pay at least a week in advance, and 2) Parents must pay for the last two weeks in advance.
- Put in your contract that parents are required to give you at least a two-week notice and that you can "terminate the contract at will."

Marketing

- Identify at least three benefits of your program. A benefit is something that will directly help a child or parent: “My program’s planned activities are geared towards each child’s interests.”
- Offer a finder’s fee for current families if they refer a new parent to your program.
- Print out business cards and flyers and pass them out. Vistaprint (www.vistaprint.org) has very inexpensive prices.

Insurance

- Contact your homeowner’s insurance agent to make sure your house and contents are covered while using them in your business. Get it in writing.
- Contact your car insurance agent to make sure your insurance covers you every time you use your car for your business. Get it in writing.
- Purchase professional business liability insurance. Get coverage for $1 million per occurrence and $2 million aggregate.

Money Management

- Pay off any credit card debt as soon as possible.
- Save at least 10% of your profit towards your retirement.
- Establish a Roth IRA by investing in a stock market Index Fund that tracks the Wilshire 5,000 benchmark.

Taking care of children is only half your job. The other half is taking care of your business. The above checklist will get you headed in the right direction.

Tom Copeland – www.tomcopelandblog.com

Going Out of Business: Non-Tax Issues

If you are planning to go out of the family child care business, you may find that quitting your business is more complicated than you might imagine.

Here is a checklist of non-tax issues to consider when ending your business.

When you have decided to go out of business, you can stop at any time - At the end of a month, the end of the week, or on any day of the week.

Contact your child care licensor, your local Child Care Resource and Referral agency and your family child care association so they can update their records.

Contact your insurance agent for your home and car. You may be entitled to a reduced insurance rate, depending on your circumstances.

Contact your business liability insurance agent. You may get a refund for cancelling your insurance policy before the end of the year. Save a copy of your insurance policy until the youngest child in your program (at the time you closed your business) reaches age 21. Before then, it may be possible for a child to sue you for an injury that occurred while in your care.

Notify your parents, in writing, that you are closing your business. Keep copies of this notice for your records. If your contract requires you to give parents a two-week notice, do so. But, if you tell parents months in advance that you are closing your business, some parents may want to terminate earlier. Take this into consideration when deciding when to inform parents of your decision.

Tom Copeland – www.tomcopelandblog.com

Going Out of Business Checklist: Tax Issues

Here is a checklist of tax issues to consider when ending your business.

1. Claim all your business income and expenses for the months you were in business when you file your IRS Form Schedule C at tax time.
2. When you file your IRS Form 8829 Expenses for Business Use of Your Home, calculate your Time-Space Percentage based on the number of months in the year you were in business. In most cases this will mean your Time-Space Percentage will not change. But, the amount of expenses you claim will be lower because you will only be claiming them for the months you were in business.
3. In the year you go out of business, the rules change for items you have been depreciating (home, home improvements, furniture, appliances, etc.). You are entitled to claim only part of a normal year's worth of depreciation. For personal property items (furniture, appliances, computer, TV, DVD player, etc.), you will be able to deduct one-half of a normal year's worth of depreciation. For your home and home improvements, your depreciation deduction will be based on the month you quit your business.
4. If you paid employees in the year you went out of business, you will need to check a box on the next quarterly Form 941 (to report social security and Medicare withholding) that is due after your business ends. The box you check will indicate that this is the last Form 941 you will be filing. If you don't do this, the IRS will continue to think that you have employees and they will expect you to continue filing this form. You must still file Form 940, W-2 and W-3 at the end of the year.
5. After filing your Schedule C and other business forms at the end of your last year in business, do not file any business forms in the next year. You do not need to indicate on your tax forms that you are going out of business.
6. If you sell any items you used in your business (toys, equipment) before you go out of business, you will probably be entitled to a business deduction. If you sell them after you go out of business, you will not be able to claim any business deductions.
7. If you give any items you used in your business to a charity (Goodwill, Salvation Army, etc.), you can only claim a charitable deduction on the amount that you have not previously deducted or depreciated as a business expense. In other words, if you bought an $80 toy and deducted 100% of the cost as a business expense, you will not get a charitable contribution when you give it to Goodwill.
8. If, before you go out of business, you replace items you have been depreciating (carpet, vinyl or wood floors, furniture, appliances, etc.), you will be entitled to deduct all of the remaining unclaimed depreciation on these items on your last business tax forms. For example, if you replace the carpeting in your play room before you go out of business, and it's the 4th year of depreciation, you can deduct the 5th-7th years of depreciation also. If you wait until after you go out of business to replace such items, you will not be able to deduct any of the remaining unclaimed depreciation.
9. After going out of business, the only thing you need to remember about taxes is that you will owe some taxes when you sell your home. Whether you sell your home immediately after going out of business or years later, you will owe taxes on the depreciation you claimed on your home since May 1997. (You will owe this tax whether or not you actually claimed depreciation on your home.) Therefore, when you do start to make plans to sell your home, contact a tax professional to help you deal with the tax consequences of this action.

Nobody says taxes are easy! But, by following the above rules, you may be able to claim some deductions you didn't anticipate.

You may want to print out this article and put it in your business records, so you can refer to it when you decide to close your business.

Congratulations on your family child care career! Good luck in the future.

Tom Copeland – www.tomcopelandblog.com

One of the most significant ways a family child care provider can reduce her taxes is to hire her husband and set up a Health Reimbursement Account (HRA).

These plans are also known as medical reimbursement plans or Section 105 Plans.

For every $1,000 of uninsured medical expenses your family has, you can expect to save between $250-$400 in taxes. This is because these expenses will reduce both your Social Security and federal and state income taxes.

Here's how it works: You hire your spouse or your own child to help you do work for your business (cleaning, record keeping, help caring for the children, etc.).

Once you set up an HRA, you can claim a business deduction for your uninsured medical expenses such as medical insurance premiums paid by your husband at work, drugs, co-payments, diagnostic fees, examination fees, hospital bills, orthodontia, braces, hearing aids, wheelchairs, eyeglasses, contact lenses, etc.

Without an HRA

Let's say your family spent $6,000 on health insurance premiums and another $4,000 on out-of-pocket medical expenses. If you were not eligible to purchase health insurance through your husband's employer ,you could deduct half of the $6,000 on your Form 1040 as a personal health insurance deduction.*

If you were in the 12% federal income tax bracket, this would save you $360 in federal taxes ($6,000 x 50% = $3,000 x 12%). The $4,000 in other medical expenses could only be deducted as an itemized expense on Schedule A to the extent they exceeded 10% of your adjusted gross income. Because of this and because of the higher standard deduction in 2019, most providers wouldn't be able to claim any medical expenses on Schedule A.

With an HRA

However, if you establish an HRA, you could deduct the entire $10,000 as a business expense. This would save you 12% or 22% in federal income taxes (depending on your tax bracket) and 15.3% in Social Security/Medicare taxes, or $2,730 to $3,730 ($10,000 x 12%/22% x 15.3%). If your state income tax was 5%, you would save another $500.

Here's a helpful brochure that includes a worksheet so you can estimate how much you would save.

Here's a flyer with more information.

The largest company that offers HRA plans is Total Administrative Services (TASC). Their HRA plan is called BizPlan. They have posted several informational videos here and here that explain BizPlan.

10% Discount!

You can receive a 10% discount on the first year's cost of BizPlan (about $400 – 100% tax deductible) if you use this application form or mention my name and code TOMA when you enroll. The person to contact for more information is Julia Cordio; Julia.Cordio@tasconline.com; 608-852-8524.

I will receive some compensation from BizPlan if you take advantage of this discount. I decided to endorse BizPlan because they are the leader in providing HRA services to family child care providers and I have been in contact with them for many years.

Pay Wages?

BizPlan includes an audit protection guarantee and an employee payroll service. Although you are not required by law to pay your spouse wages to take advantage of the tax benefits of an HRA, BizPlan strongly recommends that you pay your spouse at least a minimal amount. If you choose not to pay wages, you will not be covered under their audit protection plan.

I won a US Tax Court case for a family child care provider who did not pay wages. There has also been an appeals court case (Shellito v. Commissioner) that says the same thing.

If your family has medical expenses of at least $1,000 a year that are not covered by medical insurance, you should seriously consider setting up an HRA.

* If you are eligible to be covered through your husband's employer, you can't deduct any of the insurance premiums.

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How can a family child care provider turn “small money” into “big money”?

The secret is to start saving *now* – because when it comes to saving for retirement, time really *is* money.

The reason for this is that the more time you have to save money, the faster it will accumulate each year. For example, if you invest $5,000 and it earns 6% a year, at the end of the first year you will have $5,300 ($5,000 x 1.06 = $5,300). If this investment also earns 6% the next year, then you will have $5,618 at the end of the second year ($5,300 x 1.06 = $5,618).

In this example, notice that you earned more interest in the second year than in the first year – $318 versus $300. Because of this, your effective interest rate over the 2 years was 12.4%, rather than the 12% you would get by just multiplying 6% by 2 years.

This happened because in the second year you were earning interest on the previous year’s interest. Earning interest on interest is called **compound interest.**

Although the difference made by compounding may look small in this example, as the years pass, the compound interest on your investments will grow exponentially, earning far more than you might think is possible.

Let’s look at an example of the power of compound interest:

- Starting at age 35, Faye Provider saves $2,000 a year for ten years, investing a total of $20,000. Although she stops contributing, her investments continue to grow, earning 8% per year. After 30 years, at age 65, she will have $135,042 in her retirement account.
- Starting at age 45, Faye’s twin brother Fred saves $2,000 a year for 20 years, investing a total of $40,000. His investments also earn 8% per year. At age 65, he will have $91,524 in his retirement account.

Although Fred saved twice as much as Faye, he ended up with about one-third less money than she did when they both reached age 65. The reason for this shortfall is that he waited 10 more years before he started to save!

The compounding of interest over time is what causes money to grow exponentially the longer it is invested. Because of this, the best time to start investing your money for retirement is – today! And the next best time is – tomorrow! The younger you are when you start investing, the more time your investments will have to accumulate, and the more you will benefit from compounding.

Here’s another dramatic example: If you start investing $3,000 a year on your 35th birthday and earn 8% each year, you will have $339,850 when you reach age 65.

But, if you decide to put it off and wait just one more year to start investing (until your 36th birthday), your balance at retirement would fall to $311,898. By putting off your $3,000 savings for one year, you have lost $27,952 for your retirement.

This example illustrates the high cost of procrastinating. But what if you’re not that young anymore?

Some providers who are nearer to retirement don't start investing because they figure that they just don't have enough time for it to make a difference. But it's never too late in life to begin saving!

If you are now age 52 and you start saving $50 a week in a tax-deferred investment that earns 8% per year, you will have $104,521 at age 70.

Start investing so your hard-earned money will work even harder for you.

Note: I used the example of 6% and 8% investment return in this article. Your return can be very different. Over many years, the average return of stock investments is about 10%, although most experts anticipate a lower than average return in the coming years.

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How Much Money Do You Want to Make?

You may want to know the answer to this question because you are considering raising your rates and need help in justifying higher rates. Or, you are just curious. Whatever the reason, here's the simplest way to figure this out:

First, take the number from last year's IRS Schedule C, line 31. This represents your profit from last year. It takes into account all your business income minus all your business expenses. It's your profit.

Second, take the number from last year's IRS Form 8829 Expenses For Business Use of Your Home, line 4. This represents how many hours you worked last year.

Third, divide your profit (line 31 of Schedule C) by the number of hours you worked (line 4 of Form 8829). The result is the amount you earned per hour for your work last year.

For example, if your profit was $25,000 and you worked 3,000 hours, you earned $8.33 per hour ($25,000 divided by 3,000).

Many providers underestimate how many hours they work by not carefully counting all the hours they spent on business activities in their home when children were not present. If this is the case for you, your hourly wage will be lower if you include all of these hours.

Some providers under-report their business expenses by not claiming all the expenses they are entitled to. My book Family Child Care Record Keeping Guide lists over 1,000 allowable deductions.

How can you use this information?

If you want to raise your hourly wage, multiply the hourly wage you want by line 4 on Form 8829 to see what your profit must be. So, in the above example, if you want to earn $10 an hour, multiply $10 by 3,000 hours = $30,000 profit.

To reach this goal you would need to earn an additional $5,000 per year. If you care for four children, you could raise your rates by $1,250 per year or $24 per week. Or, you could cut our business expenses by $5,000 per year.

Sometimes parents look at how much they pay you, see how many other children are in your care and assume you are earning a lot more money than you really are. The next time parents question your rates, tell them how much you make per hour.

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Family child care providers who rent their home or apartment may face unexpected barriers to operating their business.

Their lease may include restrictive language prohibiting businesses or their landlord may withhold permission needed for a provider to get her license.

Here's some ideas for how to address landlord opposition.

Identify the reason for the opposition

There can be many different reasons why a landlord might oppose family child care providers as tenants. It's best to find out the one or more reasons upfront by asking the landlord, "What is the problem?" Oftentimes, when the issues are examined closely, there really isn't a problem. Explaining what family child care is, and is not, can go a long way to resolving conflicts.

These are the objections I've heard and how to respond to them:

A. Too many children

Sometimes landlords don't understand the difference between a center and a family child care provider. They might imagine hordes of children roaming the hallways and entryways. Make it clear how many children you have or will be in your care.

Don't cite the maximum number of children allowed under your license if you intend to care for fewer children. You may want to seek agreement with the landlord on a cap on how many children (other than your own) that could be in the apartment at one time. In some situations, a provider who is caring for only a few children should be looked at like a large family. Landlords rent to large families all the time. If the landlord is concerned about damage to the apartment because of the number of children, he/she can impose a damage deposit to address this.

B. Liability

The landlord may be worried about lawsuits against him/her arising out of more children on the premises. If you have business liability insurance, it's usually a simple matter to add the landlord as an "additional insured" under the insurance policy. This will provide coverage for the landlord at little or no cost to you.

Landlords already have liability insurance to defend themselves against lawsuits. I think this concern is overblown. I don't know of any lawsuits by parents against landlords when their child is injured in an apartment. If you don't have business liability insurance, you should get it. A provider who cares for only a few children and is not required to be licensed usually can't get business liability insurance, yet landlords generally don't object to such providers.

C. Noise

More children may mean more noise during the day, but not at night (when this might be an issue). If this is raised as an issue, you could agree to some common-sense practices: asking parents to keep noise down when dropping off and picking up, closing windows, scheduling outside activities for time that are the least disruptive, etc.

Noise usually only comes up if there have been previous complaints from neighbors about this. If so, you should try to negotiate directly with the neighbor to try to resolve the problem. If there haven't been complaints, you could suggest that the landlord monitor this issue for the next six months and try to address any issue that might arise during that time.

D. Legal barriers

Under most state laws, landlords can restrict family child care providers from operating in their apartment complex. Usually, such restrictions are found in the lease which might prohibit business use. Such restrictions are to ensure that the property can be enjoyed as a residence. While it's reasonable to have lease restrictions that prohibit fast food operations, printing presses and other commercial activities, running a family child care home can be distinguished from all other businesses.

Providers are using the apartment as a family would. There are no real noise or other issues associated with typical businesses. There are probably other home-based businesses already operating in the apartment complex, so they shouldn't single out family child care. Federally owned subsidized housing units (HUD) have, in the past, allowed family child care providers to operate even though there may be general restrictions against businesses.

Identify the benefits of a family child care provider as a tenant

Having a family child care provider in the apartment complex is not a deterrent or "problem." Rather it is a benefit to the landlord. Here are some examples of the benefits of having a family child care provider in an apartment building:

- A provider who is at home all day serves as an informal "neighborhood watch" because she is around to see what is going on in the apartment complex. Other tenants who are gone during the day should feel more comfortable knowing that someone is there to watch out for strangers and keep an eye on things.
- A provider is licensed and therefore meets a number of health and safety standards. This means that the children in her apartment may be safer than a child in their own home. I would identify several of the specific health/safety standards to show why it's unlikely that children will be at risk: first aid training, fire extinguishers, smoke detectors, criminal back ground checks, licensing/fire inspections, etc.
- A family child care provider is likely to be a more stable tenant than most because she is self- employed. She has created her own business and is committed to doing the work as shown by getting licensed.
- The apartment complex will attract prospective tenants who have families with young children. Most families prefer to use a child care provider who is close to their own home. Having a provider in the apartment complex is therefore an added benefit. If I was a landlord, I'd advertise the fact that there is a family child care provider in the apartment complex! Providers who already care for families that live in the apartment complex should point this out as evidence that they are offering a benefit to other tenants.

Before you buy or lease a home or apartment, check to see if there are any deed restrictions or objections from the landlord.

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How to Avoid Making a Big Mistake on Your Tax Return

Separating out your 100% business expenses from those that are both business and personal is one of the most important things a family child care provider can do to avoid mistakes on their tax return.

Failure to do this can mean you pay too much or too little in taxes.

It's a mistake that can easily be made if you use a tax preparer, tax preparation software, and even if you do your own taxes.

Let's use the expense of Supplies to illustrate this point. Every child care provider spends money on supplies each year: cleaning supplies, arts and craft supplies, kitchen supplies, etc.

Example

Paula Provider spends the following on supplies this year:

$300 on supplies used 100% for her business

$1,000 on supplies used by her business and her family

$400 on supplies used 100% by her family

Total spent on supplies: $1,700

Let's assume Paula's Time-Space % is 40%. How much can she deduct for supplies?

The answer is: $700.

Here's how we arrive at this number: $1,000 shared supplies x 40% Time-Space % = $400. Add to that the $300 of 100% business supplies = $700. She can't deduct any supplies used only by her family.

The Problem

If Paul had not identified which of the above three categories to put her supplies in, she would not be able to file an accurate tax return.

If her tax preparer asked, "What did you spend on supplies?" her answer would be $1,700. If the tax preparer claimed that amount on her tax return Paula would be paying too little in taxes. If the tax preparer multiplied this number by her Time-Space % ($1,700 x 40% = $680) and deducted $680, Paula would pay too much in taxes.

The correct question your tax preparer should ask is, "How much did you spend on supplies used 100% for your business? How much did you spend on supplies that were used by your business and your family?"

These same questions should be asked by tax preparers for many other expense categories: toys, repairs, office expenses, household items, and so on.

If your tax preparer is not asking these two questions, make sure you identify your expenses as either 100% or shared when you give numbers to your tax preparer.

If you are doing your own taxes, you need to understand the above example to come up with the correct deductions on your tax return.

Tax Software

Tax software (Turbo Tax, H&R Block at Home, etc.) will not help you determine the accurate amount of your expenses for supplies (or many other items). It will simply ask you to enter an amount for supplies. It won't ask you for 100% business and shared items separately. It will assume everything you buy is 100% business!

You must do your own calculation on a separate piece of paper and then enter the correct amount into the program. Unless you know how to do the calculation as I've described above, you will make a mistake.

Therefore, my advice has always been if you don't understand how to separate and identify your 100% expenses and shared expenses, you shouldn't use tax software.

Record Keeping

If Paula had not kept track of which of her supplies she had used 100% for her business and assumed that all of her non-personal supplies were business and personal, she would have claimed a deduction of $520 ($1,300 x 40%), rather than the correct amount of $700. This is a loss of $180 in deductions.

Therefore, it's very important to be keeping track of all items you are buying that are used 100% for your business. Before storing your receipts, mark them with a "B" or "100%" next to these items.

If you haven't been doing this in the past, start doing so now. It will save you a lot of money at tax time.

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How to Calculate An Actual Business Use Percent

"Can I deduct a higher percentage than my Time-Space Percentage of the cost of my swing set? I care for five children and have one of my own. My Time-Space Percentage is 40%."

The answer is yes.

How much of an item you can deduct in your family child care business depends on how much you use it in your business. If you don't use an item for your business, you can't deduct any of the cost. If you use an item 100% of the time for your business, you can deduct 100% of the cost.

What about when the item purchased is used personally as well as for your business?

The general answer is to use your Time-Space Percentage on such shared items to determine your business deduction. There are hundreds and hundreds of items that child care providers apply their Time-Space Percentage to: furniture, appliances, property tax, chairs, beds, cleaning supplies, toys, lawn mower, paper towels, light bulbs, and so on.

Some of these shared items may be used less for your business than your Time-Space Percentage and some may be used more. But, IRS rules allow you to use your Time-Space Percentage for all shared items, rather than taking the time to figure out the actual business use percent of each item.

However, you are not required to use your Time-Space Percentage on all your shared expenses.

If some items are used less than 100% for your business, but a lot more than your Time-Space Percentage, you can use an actual business use percent to determine your deduction. How do you calculate this?

Let's look at a swing set example.

The best way to calculate your actual business use percent is to track the business use for one or two months. Your records show that your five-day care children and your own child use the swing set one hour a day, five days a week. In addition, your own child uses it two hours a week on weekends. So, there were 25 hours a week of business use (five-day care children x one hour a day x five days) and 7 hours a week personal use, for a total of 32 hours a week. 25 divided by 32 = 78% business use.

If the swing set cost $1,000, you could deduct $780 of the cost.

It's important to keep some records showing your actual business use. Don't guestimate this. If, in this example, you said your business use was 75%, without having tracked any actual use of the swing set, you will have a hard time defending your percentage in an IRA audit.

Try to track the actual use for at least a month (preferably two). It makes the most sense to use an actual business use percent for items that cost hundreds of dollars and are used a lot more than your Time-Space Percentage. Don't try using an actual business use percent for your toilet paper!

You can use the Time-Space Percentage for most of your items and an actual business use percent for those selected items that are used heavily for your business.

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"Must I count the space in my basement and garage?"

"Can I count my downstairs room if licensing rules prohibit me from having day care children downstairs?"

"Can I count my own child's bedroom if he takes a nap in it every day, but day care children do not enter the room?"

What are these family child care providers asking about?

The Time-Space Percentage (T/S%) is the single most important number for you to accurately calculate because it will make the biggest difference in reducing your taxes.

Your T/S% represents the portion of your home that is used for business purposes. You will use it to determine how much of the thousands of dollars of your house-related expenses you can deduct.

To calculate your T/S%, you must first calculate your Time Percent and then your Space Percent. See other articles on these topics.

The Space Percent

Your Space Percent is calculated by dividing the number of square feet in your home used on a regular basis for your business by the total number of square feet in your home.

Look at each room in your home and ask, "Am I using this room on a regular basis for my business?" If the answer is yes, count all the square feet in the room; if no, don't count any of the square feet. Your living room, dining room, kitchen, bathroom, entryway, playroom, and pantry are probably all regularly used in your business. A bedroom used by children for naps 30 minutes each day is considered regular use. Using a room 2-3 times a week is probably regular use.

You must count your basement and garage as part of the total square feet of your home.

If your state licensing rules prohibit you from bringing children into your basement, you may still be able to count the basement space as regular use if it contains a furnace area, laundry room, or storage area for household items used in your business (tools, household supplies, etc.). Children don't have to be in a room for the room to be considered as regular use.

If you use your garage to store a car used for your business, tools, bikes, garbage can, recycling, garden supplies, etc., you could consider your garage as regular use.

Rooms that would not be considered as regular use would be a bedroom never used by the day care children, a personal bathroom never used by the children, or a gun room.

Most providers count all the rooms in their home as regular use and therefore their Space Percent would be 100%. Don't be afraid to claim a 100% Space Percent!

After calculating your Space Percent, multiply it by your Time Percent to get your T/S%. Most providers who work full-time, year-round will probably have a T/S% of between 30-45%. You must recalculate your T/S% each year.

Enter your Space Percent on Part I of IRS Form 8829 Expenses for Business Use of Your Home.

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"Can I count the hours I spend cleaning my home?"

"Can I count the hours I spend on the Internet?"

"Can I count the hours I spend at a workshop on child development?"

What are these family child care providers asking about?

Time is money. This is particularly true for family child care providers because the more time you work in your home, the lower your taxes. The hours you work are used as part of a formula called the Time-Space Percentage (T/S%) that determines how much of your home you can deduct as a business expense.

You want to make sure your T/S% is accurate because it will be applied to thousands of dollars' worth of expenses: property tax, mortgage interest, house insurance, utilities, house depreciation, toys, furniture, appliances, and much more.

To calculate your T/S%, you must first calculate your Time Percent and then your Space Percent.

The Time Percent

This percent is determined by adding up the number of hours you are using your home for business purposes and dividing this number by the total number of hours in the year (8,760). There are two types of hours to include: hours when day care children are present in your home and hours when children are not present, but you are engaged in business activities.

Hours when children are present in your home

Count hours from the moment the first child arrives until the last child leaves. Don't count the hours of operation as reflected in your contract; instead, keep records of the actual hours children are present. If you care for children from 7 am to 5:30 pm, that's ten and a half hours a day or 31% of the week. If your pick-up time is 5:30 pm but the last parent usually leaves closer to 6:00 pm, count this extra time. A half hour a day every day is equal to 1.5% of the year, which is significant when applied to all your house expenses.

Hours when children are not present in your home

Count all hours spent on business activities such as: cleaning, meal preparation, activity preparation, record keeping, parent interviews, parent phone calls, time spent on the Internet, and so on. Such activities may be done by your spouse (cleaning toys) or by your own children (laundry). Don't count time spent away from your home, even if you are engaged in a business activity (training workshop, transporting day care children).

Tracking your hours

Keeping track of your attendance hours is relatively simple; tracking the hours you work when children are gone requires more effort. Try to keep a daily record of all the hours you work when children are gone for at least two months each year. Use the average hours worked for these two months for the rest of the year. Mark this time on a calendar and note what time of day you did the work.

Carefully tracking the hours you work after children are gone is perhaps the most important thing you can do to reduce your taxes. Most child care providers underestimate these hours and pay higher taxes as a result. Everyone and a half hours of work each week is equal to a rise of about 1% in your Time-Space Percentage. Although this might seem like a small amount, it's not when applied to thousands of dollars of house expenses.

The average amount of time providers care for children is about eleven hours a day, five days a week. This is equal to 33% of the year. The average amount of time child care providers conduct business activities after the children are gone is about 14 hours a week, or about 8% of the year. Therefore, a typical child care provider's Time Percent is around 40%. Yours may be higher or lower.

Enter your Time Percent on Part I of IRS Form 8829 Expenses for Business Use of Your Home.

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How to Claim Expenses When You Do Child Care Away From Your Home

In many states family child care providers run their business out of a home they don't live.

There are a number of reasons why they do this:

- Some don't want to disrupt the space where their family lives.
- Some can't get their own homes licensed because of building or fire codes.
- Some find a different location is a better place to attract new clients.

Whatever the reason, how do you claim business expenses when you don't live in the space you are doing child care?

If you are only using the separate location for business purposes (no personal parties on the weekends!) then you are entitled to deduct 100% of the cost's association with the space.

This includes rent, furniture, appliances, renter's insurance, food, toys, supplies, utilities, and so on. Everything. This is true whether you rent your place of business or own it.

If you are using the separate location for some personal activities, then calculate your actual business use percent of your business expenses.

Claim all of these expenses on IRS Form Schedule C Profit or Loss From Business. Sometimes there can be confusion about what expenses to claim on Schedule C or IRS Form 8829 Expenses for Business Use of Your Home. This is because there are some expenses that appear on both forms (mortgage interest, insurance, rent, repairs and maintenance, taxes and utilities).

If you live in your home where you do child care, you must claim your house expenses on Form 8829. These include property tax, mortgage interest, house insurance, utilities, house repairs and home depreciation. You claim your remaining business expenses on Schedule C.

If you don't live in the home where you do business, you do not fill out Form 8829. Instead, claim everything on Schedule C.

Car expenses

You can claim car expenses when you take trips that are primarily for your business. This includes trips to the grocery store, bank, field trips, and so on. However, if you do child care in a separate home you cannot claim the miles traveled between your home and your place of business. This is considered commuting and it's not deductible.

If you travel to and from your business location primarily for business purposes, you can claim these miles. In the same way you can count trips to and from your home for business purposes.

Other

You cannot claim the Time-Space Percentage of the expenses of the home you live in if you do child care in a different location. But, you can claim expenses for things in the home you live in that you use for your business. Examples are a computer, printer, copier, desk, file cabinet, washer/dryer, etc. For these items, calculate an actual business use percent.

Here's how to calculate your house expenses when doing child care out of two different homes in one year.

Although we don't have the final regulations from the IRS on this point, it's likely that providers who do child care out of a separate home will not be better off using the new IRS safe harbor rule for claiming house expenses.

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The biggest single expense for many family child care providers is food. Therefore, you want to make sure you claim this deduction accurately.

You have two choices in how to claim food expenses:

The Standard Meal Allowance Rule

This rule allows you to claim food expenses without saving any food receipts! I lobbied the IRS to adopt this rule in 2003 (IRS Revenue Ruling 2003-22) because I saw how difficult it was for child care providers to save receipts for all business and personal food and try to sort out which was which.

To use this method, add up all the breakfasts, lunches, suppers, and snacks you serve to the children in your care and multiply by the standard meal allowance rate for 2021/2022: $1.39 breakfast ($1.40 2022), $2.61 lunch/supper ($2.63 2022), $.78 snack ($.78 2022). The rates are higher for Alaska and Hawaii. You can deduct up to one breakfast, one lunch, one supper, and three snacks per day per child (if you serve that many!). Some providers get confused about this because the Food Program will only reimburse up to three servings per day per child. See my "Deduct 6 Meals?" blog post.

All child care providers can use the standard meal allowance rule to claim food expenses whether or not they are on the Food Program, and whether or not they are operating legally.

If you use this rule, the main issue is to keep the following records: name of each child, dates and hours of attendance in care, and the number of breakfasts, lunches, suppers, and snacks you served. If you are on the Food Program, keep your monthly claim form that contains this information.

What's most important, however, is to keep a daily record of all meals and snacks that are not reimbursed by the Food Program. You don't need to keep a menu. These non-reimbursed meals and snacks do not have to be nutritious. If you serve a popsicle in the afternoon, it's a snack! I'm not advocating that you serve junk food, but if you do, it's deductible. Do your best to record these non-reimbursable meals and snacks because it adds up: One non-reimbursed snack a day is worth $203 a year per child!

Actual Food Cost Method

If you use this method, you must save receipts for all your business and personal food. Saving all personal food receipts can be a chore. You must do this, however, so that the IRS will believe that your business food receipts are for your business.

You can use several different ways to estimate the actual cost of the food served to the children in your program. You could buy food separately, calculate your own average cost per meal, or deduct a percentage of the total cost of your food. My book Family Child Care Record Keeping Guide lists six ways to determine your food costs using this method. In addition to all your food receipts, you must also keep the same records described above when using the standard meal allowance rule.

Because of the extra work required by this method, most child care providers use the standard meal allowance rule.

Note: Any food eaten by you or your own children at home is not deductible no matter which method you use to deduct food expenses.

Claim your food expenses on Schedule C as “Other Expenses” on line 27. See my previous blog post “Are CACFP Reimbursements Taxable Income?”

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Which of the following rooms can a family child care provider claim under the exclusive use rule?

A downstairs room where day care children play that also contains a coat closet that the child care provider's family uses.

A remodeled garage that is turned into a children's play room. The child care provider has no children of her own living at home.

A children's play room that is by the day care children. The child care provider has young children of her own that use the room only during child care hours.

Answers: B and C.

Family child care providers can substantially increase their Time-Space Percentage (T/S%) if they have one or more rooms that are exclusively used for their business. An exclusive use room is a room that is never, ever used personally. This is a strict rule. If you use the room even once during the year for personal purposes, you cannot take advantage of this rule. Don't try to use this rule unless you are absolutely certain you qualify.

Here's an example of how this rule works.

Let's say your home is 2,000 square feet and you have an exclusive use room that is 200 square feet. The rest of the home is regularly used for your business. Your Time Percent is 40%.

Step One: Calculate the business use percentage of the exclusive use room:

200 square feet divided by 2,000 square feet = 10%

Step Two: Calculate the T/S% of the rest of the home:

1,800 square feet of regular use space divided by 2,000 square feet = 90% Space

90% Space x 40% Time = 36%

Step Three: Add the totals from Step One and Two together:

10% + 36% = 46% T/S%

Note: If you had used the 200 square foot room only regularly for your business, your T/S% would have been 40% (100% Space x 40% Time). Applying the exclusive use room increased your T/S% by 6%, which is significant!

The Instructions to IRS Form 8829 tells child care providers to do this calculation on a separate piece of paper and then attach it to the form. Enter the T/S% on line 7 of Form 8829.

Family child care providers are the only home-based business that can have both regular use rooms and exclusive use rooms. If you have such a room, be sure to take advantage of it as this will significantly decrease your taxes.

Take pictures of the room to help you prove that you had an exclusive use room if you are audited. If you have young children of your own take pictures of your children's bedrooms and toys so the auditor can see that they do not need to enter the exclusive use room after the day care children are gone.

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A new child care center just opened in your neighborhood. It offers care for a hundred children (toddlers through school-age) and has a well-equipped playground, a van to transport children, and sparkling classrooms with bright furniture and plenty of toys.

You start to feel desperate, wondering if you'll ever be able to fill your two openings. "How can I compete?" you ask yourself.

In some ways, child care centers have an advantage over family child care. They are easier to find, they have a full staff, their buildings are easily accessible to the public, and they can spend money on advertising.

Some parents are afraid to use family child care providers because providers are alone in their home, and parents worry about what goes on behind closed doors.

For these reasons, providers need to work hard to counteract parents' fears. Here are some suggestions for how to compete:

- Visit your local child care center(s) and get copies of all written materials given out to prospective clients (rate schedules, special services, discounts, etc.). See what additional information you can see on their website and watch for any ads they may be running in local newspapers or online. Prospective clients contacting you may be comparing what you offer with what this center offers, so you need to be informed.
- Look over the materials you have collected. Think about how your program is different from the center. What do you offer that the center does not? Your answer might include some of these benefits:
    - Small group size which allows for more individual attention to help children learn
    - Home environment where children can play in familiar, comfortable surroundings
    - Home-cooked, individually prepared meals
    - Healthy environment for children because fewer illnesses are spread in a small group
    - Longer or more flexible hours
    - Consistent caregiver (staff turnover at centers is usually high)
    - Mixed age groups, allowing siblings to be together
    - Accreditation or child care credentials

Remember, your program may never have everything a center offers, but you will always have some benefits that a center does not have.

- Promote your program by highlighting your benefits. Distribute door hangers or flyers in your neighborhood. Offer a discount on the first week of care.
- Offer your current clients a finder's fee if they refer a parent who enrolls with you.
- Introduce yourself to the director of the center. Suggest ways you might cooperate. If the center doesn't offer infant care and you do, ask if the center will refer parents with infants to

you. Offer to provide backup care for the center for mildly ill children. Offer to provide drop-in care for center clients who need care after the center closes.

You need not fear the competition from a child care center if you can effectively communicate the benefits of your program.

Tom Copeland – www.tomcopelandblog.com

It's not easy trying to attract new parents to enroll in your family child care program.

You are competing against other family child care providers, child care centers, school-age programs, Head Start, and unregulated caregivers.

When competing against unregulated caregivers, you have some special challenges.

I am defining unregulated caregivers (also called exempt care, kith and kin, relative care or informal providers) as those who are not in violation of state child care licensing rules. They don't have to follow all of the regulations that a licensed family child care provider must follow.

I'm not talking about child care programs that operate illegally, in violation of licensing rules. I believe illegal providers should be convinced to become regulated or they should be forced to shut down.

Parents use unregulated caregivers for many reasons: it's usually cheaper, it may be provided by a relative, or they may know the caregiver from their community. Some parents don't know the difference between regulated and unregulated care.

You should assume that when a parent looking for child care contacts you, she is also considering using an unregulated caregiver.

Here are some suggestions for how to compete against unregulated caregivers:

Safety – Parents' number one concern about child care is safety. Therefore, when talking to prospective parents you should emphasize that being regulated means you and your home have passed a series of safety tests, including criminal background checks, first aid and CPR training, fire department inspections of your home, and adherence to safety standards, such as the proper storage of hazardous materials in your home.

Say to the parent, *"If you are considering enrolling your child in another home, ask if that caregiver is licensed. If not, ask if they are trained in CPR and first aid? Do they have any history of criminal activity or sexual abuse? Do they have an emergency evacuation plan?"*

Fees – Informal caregivers probably charge less, perhaps significantly less, than you. Do not try to compete on the basis of price. There will always be providers with lower rates than yours, and you can be successful even while charging higher rates.

Say to the parent, *"If you are looking for the cheapest care in town, that's not me. My rates are based on the quality of care I offer and the safe and healthy environment I provide for your child."*

Value – Stress the value of your services by promoting the benefits of your program. Tell the parent what advantages you offer to children that unregulated programs don't offer.

Say to the parent:

"I offer a variety of planned learning and play activities that will help your child be ready to succeed in school."

"I have specialized training in child development so I can respond quickly to meet your child's needs."

"I offer special services (piano lessons, second-language exposure, numerous field trips, computers, etc.) that will enrich your child's education."

Conclusion

Parents who can see that you offer high-quality child care will pay for it. It's your job to show them.

You can't appeal to every parent. Some will always pick the cheapest care. Let those parents go. People usually get what they pay for. Parents who pay bargain-basement rates will get bargain-basement care.

Tom Copeland – www.tomcopelandblog.com

What is a Profit/Loss Statement and how can a family child care provider make use of one?

A Profit/Loss Statement is a financial statement that summarizes your income and expenses for a specific period of time. You can prepare such a statement monthly, quarterly or annually.

Your annual Profit/Loss Statement is the IRS Form 1040 Schedule C Profit or Loss From Business that you file each year with your tax forms. This form shows your income and all your business expenses. The bottom line of this form, line 31, represents your profit (or loss).

What use can you make of a Profit/Loss Statement?

If you want to borrow money to buy or refinance your home or make a home improvement, the bank will want to examine your Schedule C to see whether your profit can justify the loan. However, your Schedule C is not an accurate reflection of your ability to pay back a loan.

Instead, you may want you to prepare a monthly or quarterly Profit/Loss Statement that shows your actual income and expenses for that period. When you add the monthly loan payment to the list of expenses, you can more easily show the bank that you can afford to pay the loan back.

Sometimes providers need to show a Profit/Loss Statement if they are applying for a grant, or as a requirement for participating in a training program. Or, such a statement can be a helpful part of a general business plan.

Even if you are not required to create a Profit/Loss Statement, it's a useful exercise to help you track your financial progress over time, spot problems (too little income, too many expenses) early on and take steps to address them.

I think it can be helpful to look at your Schedule C each year and compare it to previous years. Ideally, you want your income to increase and your expenses to decrease over time. This will result in bigger profits and more money for you to meet your own financial goals.

Example of a Profit/Loss Statement

The basic content of a Profit/Loss Statement is a breakdown of your sources of income and expenses. As we have said, your Schedule C is such a statement for the year. To create a Profit/Loss Statement for a month or quarter requires some additional work.

It's relatively easy to record your income for any particular month or quarter. Your income will include parent tuition and fees, CACFP reimbursements, subsidy payments, and grants.

Some expenses are easy to track by month or quarter. Other expenses that occur more infrequently need to be accounted for by spreading them over each month. In other words, if you pay your property taxes twice a year, you'd take the total amount and divide by twelve months and enter the monthly amount in a monthly Profit/Loss Statement. Similarly, take your annual house depreciation (or and other annual depreciation deduction) and spread it monthly.

If you use the KidKare online software program, you can use its Schedule C Worksheet to create a Profit/Loss Statement for a month, quarter, or for the year. This worksheet does not include food expenses, car expenses or depreciation deductions, so you must look at the separate reports for these expenses and add them to the Schedule C Worksheet after printing it out.

Summary

Profit/Loss Statements can be a useful tool to help you meet your financial goals. It can also be used in conjunction with a budget and cash flow statement to help you better manage your business.

Tom Copeland – www.tomcopelandblog.com

Family child care providers can deduct expenses associated with their vehicle based on the number of business miles they drive.

You can count the miles of a trip as business as long as the "primary purpose" of the trip is for your business. A trip is primarily for business purposes if more than half of the reason for the trip is business.

Taking daycare children on field trips or transporting them to or from your home can clearly be counted as a business trip. Trips to the bank to deposit parent fees, to the library to get children's books, or to training workshops also count as business trips.

What about these trips?

1. **You drive to the gas station to get gas.**

You could only count this trip as business if more than half the miles you drove your vehicle were for business purposes. This would be highly unlikely unless you had a second vehicle that you used primarily for your business.

2. **You drive to the grocery store to buy business and personal food.**

If you spent more money on business food than personal food, you can count this as a business trip. Many providers almost always buy more business food than personal food. If so, don't try to claim every trip to the grocery store as a business trip. The IRS will never allow this. Instead, if you normally spend 75% of food for your business, count 75% of your trips.

3. **You drive to school to drop off two daycare children and two of your own.**

This example is tricky. If the primary reason to go to school is to drop off the daycare children, then count this as a business trip. If the primary reason is to drop off your own children, don't count the trip. If you weren't in business and would drop off your own children anyway, don't count these trips.

Claiming Business Trips

Once you have determined whether or not your trip is a business trip, add up all the miles for your business trips.

You have two ways to claim car expenses. You can use the standard mileage method or the actual expenses method.

If you choose the standard mileage method, multiply your business miles by $.58.5 (2022 standard mileage rate). In addition, you can claim parking expenses, tolls and the business portion of your car loan interest and any personal property tax on your car.

If you use the actual expenses method, you can claim the business portion of all expenses associated with your car: gas, oil, repairs, insurance, parking, tolls, membership in AAA, car wash, depreciation, etc.

The business portion of your car expenses is determined by dividing the number of business miles by the total number of miles your drove your vehicle. For example, if you drove 3,000 business miles and 10,000 total miles, your business use is 30%. You could then deduct 30% of your vehicle loan interest and personal property tax if you use the standard mileage rate, or 30% of all your vehicle expenses if you use the actual expenses method.

If you have more than one vehicle, you can choose either method for each vehicle.

Tom Copeland – www.tomcopelandblog.com

There is a right way and wrong way to end your agreement with the parent of a child in your care.

The right way is to follow the terms of your contract. If it requires you to give parents a two-week notice, do so. You and the parent can agree to end your agreement earlier than two weeks if you put it in writing and both sign it.

Here are three tips to improve the chances that the ending of your agreement will go smoothly.

"Terminate at will"

While I recommend that you require parents to give you a two-week notice to end your contract, I also recommend that you do not restrict yourself to the same terms. Instead, put in your contract, "Provider may terminate at will." This gives you the flexibility to end your agreement immediately if the parent is threatening you, creating a disturbance for your business, or refusing to pay you for your services.

Refund payments?

You cannot charge parents for days that you refuse to provide care. Let's say you want to immediately terminate your contract with a parent. It's Friday. The parent has paid you for the past week and has paid you in advance for the last two weeks of care. If you tell the parent she can't come back on Monday, you are obligated to refund her the amount she paid you for the last two weeks.

Did you or the parent terminate care?

Sometimes there is miscommunication between a family child care provider and a parent. If you are in a conflict situation with a parent and are considering terminating care, be sure you communicate clearly. Let's say the parent owes you money for care from last month and you are struggling to collect it. Your contract requires the parent to give you a two-week notice while you may terminate "at will."

When you try to discus this payment issue today, the parent is vague about when she can pay you. You then make one or more of the following statements:

"I can't wait any longer for your payment."

"I've had enough. I don't think I can go on like this."

"You must pay me by tomorrow or I'm going to have to end our agreement."

It's possible that the parent will conclude from any of these statements that you have terminated your agreement the day of this discussion. Let's say the parent doesn't show up tomorrow and you don't hear anything more from her. Has she effectively given you a two-week notice because she hasn't returned? Did you terminate her?

If it's not your intent to terminate your contract immediately, it's important to be clear to the parent that you expect her to bring her child to your program the next day ("I'll see you and your child tomorrow.")

If you are terminating immediately, you cannot expect any payment from the parent for care after that day.

What if, in response to any of your comments above, the parent says, "I'm not coming back." If you want to be able to collect payment for the next two weeks, you need to come to an understanding that the parent is giving her two-week notice. Therefore, say to her, "Does this mean you are giving me your two-week notice?" If the parent agrees, then either write up a short note that says this and get the parent to sign it, or send the parent an email indicating that you are accepting her two-week notice.

If a parent is not showing up for care and has not given you an official notice to end your agreement, send the parent a note, asking for clarification. If you are willing to continue to provide care say, "I have not ended our contract. You are welcome to continue to bring your child to my program. If I do not hear back from you within a week, I will assume you have given me your two-week notice and I will then proceed to take legal action to collect what you owe me under our contract."

If you don't want the parent to return, say, "I'm sorry we couldn't agree to continue our agreement. I'm no longer providing care for your child." Then say either, "You owe me $ under our contract," or "I'm refunding you $ for the days you paid for care after the end of our agreement," or "You do not owe me any additional money."

The language you use is important to be clear whether you or the parent is ending your agreement.

Tom Copeland – www.tomcopelandblog.com

Do you find it difficult to enforce your contract and policies? You are not alone.

When a family child care provider starts to feel frustration and anger towards a parent, some providers prefer not to deal with the conflict at all and simply hope that it will go away. That's obviously not a solution.

Since you created your contract and policies, it is up to you to enforce them. Otherwise, they won't mean anything. You should look closely at each section of your contract and policies. If you aren't willing to terminate a parent who refuses to follow one of your rules, take it out. It's not a rule; it's a guideline that you won't enforce.

You must start by taking your contract and policies seriously. Tell parents that you will expect them to follow your rules. It's recommended that you get into the habit of bringing up all violations of your rules to show parents that you mean business.

You can listen sympathetically to a parent's concerns, but you should also make it clear what they can expect if they don't follow your rules.

To enforce the rules of your program, there must be a consequence to the parent who doesn't follow them.

The most common consequence is to charge the parent more, and the ultimate consequence is to end your contract with the parent. It's as simple as that.

So, if a parent is late to pick up their child, you can charge a late pick-up fee. After warning the parent and giving them several chances to change their behavior, you can terminate your agreement.

You can have different consequences for different parents. If your contract says parents must pay $1 a minute for late pick up, and one parent is regularly late, you can double her fee to $2 a minute.

To give yourself maximum flexibility in enforcing your contract, write in your contract, "Provider may terminate at will." This allows you to end your agreement immediately, if necessary to protect your business.

Providers sometimes worry that if they enforce their contract, the parent will leave their program. This can happen. But, it's extremely rare. If you are doing a good job of communicating with parents and offer a high-quality program, you need not worry about what will happen when you enforce your rules.

Providers who consistently enforce their rules are less likely to have to deal with parents who will try to violate them. You don't have to raise your voice or shame a parent to enforce your rules. Simply refer to your contract and policies to make your point.

If you need help enforcing your rules, ask another provider for advice. Put what you want to say to a parent in writing. You can do it!

How to Find a Tax Professional

Finding a tax professional who can file your taxes correctly can be a challenge for many family child care providers.

The reason is that there are several unique tax rules affecting providers that many tax professionals do not fully understand. These include the ability to:

1. Claim most household items as “ordinary and necessary” business expenses.
2. Claim food expenses without food receipts using the IRS standard meal allowance rule.
3. Count all the hours you work in your home, including the number of hours you work on business activities when children are not present.

The simplest way to find someone would be to talk to providers in your area and ask if they use tax professionals and if they are satisfied with them. Someone who has experience doing family child care tax returns is more likely to file an accurate tax return for you. This is not a guarantee, but it is a place to start.

You may want to look for a tax preparer who has a credential (an accountant, Enrolled Agent, or even someone who worked previously for the IRS). However, someone with a credential does not necessarily mean that they will prepare your taxes correctly. The best credential to look for is an Enrolled Agent (EA). This is someone who has passed an IRS examination and is likely to be familiar with tax issues affecting small businesses such as yours. An EA can also represent you in the event of an IRS audit. To find an Enrolled Agent, go to https://www.naea.org/ and click on “Find a Tax Expert.”

You may also want to ask your local or state family child care association or family child care union if they know of names of tax professionals who work with providers.

Tom Copeland – www.tomcopelandblog.com

How should you handle the following situations?

- First – A mother calls you up and says "My husband and I are starting divorce proceedings and I don't want him to pick up our child anymore."
- Second – At the time of enrollment, the mother tells you that she is separated, but not divorced from the father. One day a man shows up at your program saying he is the father and is there to pick up his child. The child runs to him, saying "daddy, daddy!" You've never seen this man before.
- Third – Parents have joint custody and the father picks up the child on Fridays. The father tells you his new girlfriend will be picking up the child next Friday. The mother finds out and says she doesn't want girlfriends picking up her child.

What a hassle!

It can be stressful when you find yourself being forced to act as a referee in disputes between parents.

These parent disputes can get intense and many providers wonder how they can avoid being caught in the middle.

Here is the general rule. Biological parents have equal rights to their children unless a court has limited their rights.

This means a mother can't limit the rights of a father or vice versa. So, in situation #1, if mother doesn't want the father to pick up the child, you cannot agree to this request. The mother must have some kind of court order before you can limit the ability of the father to pick up the child. A court order can be a divorce decree, order for protection, custody order, or restraining order. Therefore, you would say to this mother, "I'm sorry but the father will be allowed to pick up the child until I have a copy of a court order that says he can't."

If you refuse to give up the child to the father, it can be considered kidnapping.

What if the mother says she just received a court order giving her full custody of the child? You should reply, "Great. Send me a copy by fax, email or letter. But if the father shows up before I receive a copy, he will be allowed to take the child." You should never take the word of a parent in this situation. Always allow the child to go with the biological parent until you have a copy of a court order.

In situation #2, you don't know that the man picking up the child is the father. So, you should say to him, "I don't want you to take the child because I don't know who you are. Have a seat while I try to contact the mother." If the man insists on taking the child, call 911. Do not lock the child in a back room and refuse to allow the man to take the child. Do not pull out a baseball bat and wave it at the father, as one provider told me she does. No! Think of the liability issues. Try to resolve the problem peacefully, but don't put yourself or children at risk. Let the police sort it out.

In situation #3 you have three choices. The father wants his girlfriend to pick up and the mother objects. First choice – tell the mother and father that they each get to decide who to put on their own list of authorized people who can pick up their child. Neither party can veto the names on the other person's list. If the girlfriend is on the father's list, she can pick up.

Second choice – Tell the parents they must come to an agreement and present to you one list of who is authorized to pick up the child on each day.

Third choice – Who do you like better? If you like the mother better, you can tell the father he can't have his girlfriend pick up. Can you do this? Yes! Since the girlfriend is not the biological parent, she has no rights to the child.

In my opinion, choice #1 is the best option. Each parent should have the right to determine who can pick up on their day.

In summary, follow what a court order says. If you are not clear about what it says, ask the parent for clarification. If two parents don't agree as to what the court order says, tell them you will call the police and ask them to sort it out unless they can agree.

I've talked with many family child care providers and child care center workers who find themselves in the middle of bitter custody fights between fathers and mothers. By following these guidelines, you can reduce the stress on you and the child.

Tom Copeland – www.tomcopelandblog.com

How would you handle these situations?

- A pregnant parent calls and wants to enroll her infant in your family child care program four months from now.
- A current parent will be staying home with her child during the summer and wants to bring her child back to your program in the fall.

I have heard from child care providers who held an opening for several months for free, only to find out days before the care was to begin that the parent was not bringing her child. During this time, they had turned down the opportunity to care for other children and were very upset about the money they had lost.

To avoid this problem, most child care providers charge a small fee in exchange for their promise to hold the opening. Others charge a percentage of their regular rate during this time.

I strongly recommend that if you promise to hold a space for a parent, you ask them to pay for this promise. If the parent doesn't want to pay holding fees, tell the parent that you will be happy to care for their child if you have an opening when they want to return. But don't promise to hold the space. It's that simple.

What if you can't easily fill your opening?

Let's say parent Patricia Lessard wants to enroll her child in your program in September but can't afford your holding fee. If you anticipate having a difficult time filling your space, you may want to make Patricia this offer: You will continue to advertise to fill your space. If no other parent contacts you before September, Patricia can enroll her child and won't have to pay a holding fee. If another parent wants to enroll their child before September, you will agree to call Patricia first to see if she will be willing to pay a fee to hold her spot. This gives Patricia hope that she will be able to enroll her child.

How much should a provider charge to hold an opening?

Before you decide to charge a holding fee, consider what you are giving up. Let's say your normal rate is $150 a week. By holding a space for a child for three months (12 weeks), you are giving up $1,800 in income unless you charge a holding fee. If you can easily fill the opening during the holding period, then perhaps you should charge close to your full rate. If the opening will be more difficult to fill, perhaps you should charge less. But if it is hard for you to predict how easily it will be to fill your openings, consider charging 20-50% of your normal rate.

Should you apply the holding fee to the first weeks of care?

Not in my opinion. The holding fee is to compensate you for giving up the right to fill your space. You are losing a lot of income during this holding period. If you apply the holding fee to the weeks after you begin care, the parents are really getting your promise in exchange for nothing. This is not fair.

Require the parent to pay the holding fee upfront, or have them pay you a set amount each week. If they fail to make their weekly payment you should notify them that you will no longer hold the opening.

Don't call the holding fee a "deposit" because you don't want to imply that somehow the parent can get the money back. Call it a "non-refundable holding fee."

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There are advantages to hiring your own children under age 18 to help you with your family child care business.

But, there are also pitfalls you want to avoid so you won't run into trouble with the IRS.

First, the advantages:

- Your children can reduce your workload by helping you care for the day care children, cleaning up after the children, cooking, or doing a variety of other tasks.
- You can pay your children and deduct their wages as a business expense. And depending on the amount you pay, the child may not owe any taxes on what they earn. This can result is a big tax savings for your family.

Next, the pitfalls:

The IRS is naturally suspicious of family child care providers who hire their own children for their business. They assume that some child care providers are not following the rules when hiring their own children and thus are not entitled to the tax benefits.

Non-Tax Rules

- If you want to be able to deduct the amounts you pay your own children, you need to keep proper paperwork to show that the money you paid your child was for work and was not an allowance. This means:
- Prepare a job description that details the responsibilities of the job: play with the children, clean up before and after the children, prepare meals for the children, clean toys, record keeping, etc. Do not include more personal activities such as shopping, mowing the lawn, running family errands, etc. Don't count any work for any activity that would still be done if you weren't in business.
- Prepare a written agreement between you and your family member that describes the employment arrangement: days and hours of work, pay, etc. Both parties should sign this agreement.
- Keep a daily record of when the work was done. If the work done is the same every day, simply record the days and hours worked: Monday 9am – 10am, Tuesday 9am – 10am, Wednesday 9am – 10am, etc.
- Write out a receipt for each payment, get the family member to sign it, and keep a copy: "Payment of $25 cash for 5 hours of work January 3 – 7, 20__." It is not necessary to pay by check; you can pay with cash. Make this payment out of a separate business account if you have one. You could also compensate your child by buying them clothing, movie tickets or other items.
- Payments to family members must be reasonable. If you have a $15,000 business profit, it is unreasonable to pay your own children $6,000 in wages. Payment of $20 per hour to your 15-year-old is also unreasonable. The test of what is reasonable is probably how much you would be willing to pay someone who is not a family member. If you also give your child an allowance, keep a record of when you gave this allowance and how much it was. The

federal minimum wage is $7.25 per hour. Although you are not required to pay this amount, it should be considered a reasonable wage for any child.

- Federal child labor laws make it illegal to hire anyone to work for you if they are under age 14. This law doesn't apply when hiring your own children. But, check to see if your state child labor laws apply to hiring your own children.

Tax Rules

- Get a taxpayer identification number (EIN) from the IRS (Form SS-4 can be filled out online at www.irs.gov).
- You don't have to withhold any federal or state income taxes.
- If your child is under age 18, you do not have to withhold or pay Social Security/Medicare taxes.
- You don't have to pay any federal unemployment taxes. Check with your state to see if you must pay state unemployment taxes.
- If your child earns less than $12,550 (2021 amount) from all jobs they have inside or outside the home, he/she does not have to file a tax return or pay any federal income taxes.
- File IRS Form W-2 and W-3 at the end of the year to report what you paid your child. You don't pay any taxes when filing these forms. Failure to file these forms shouldn't impact your ability to deduct the wages you paid as a business expense. But filing the forms does help show the IRS that you have an employee.
- Update: Some child care providers and tax preparers file the quarterly IRS Form 941 (or the annual 944) as another way of showing that they are treating their own child as an employee. These forms are normally filed to pay Social Security/Medicare taxes. When you hire your own children under age 18, you won't owe these taxes and therefore it's not required that you file these forms. I've had some providers tell me that when they filed these forms the IRS assumed they owed money and wrote letters requesting they pay. After some correspondence, the IRS backed off. I've heard from others that they never had this problem. To be on the safe side, you may want to file these forms.
- You don't have to pay your child the federal minimum wage of $7.25 per hour. Check with your state (Department of Labor) to see if you must pay any state minimum wage.
- Check with your state to see if you must purchase workers' compensation insurance.

Conclusion

Many child care providers have their own children work for them, but don't pay them anything. It's okay not to pay your children! You can reward your children by giving them gifts or their help can be considered an expected household chore. If you do this, the gifts are not a business expense.

If you want to be able to deduct the amounts you pay your children, you must follow the rules cited above. Although the paperwork can be intimidating, the tax benefits are real.

Thanks to Alison Jacks and Kelly Nokleby.

How to Identify the Benefits of Your Child Care Program

Parents looking for a child care program today want answers to these two questions:

"Why should I bring my child to your program?"

"What does your program offer that other programs do not?"

Your ability to answer these questions will make a big difference in whether a parent chooses to enroll their child in your program or not.

Because parents have a lot of child care programs to choose from, you will need answer these questions by effectively communicating the benefits that your program offers parents and children.

To compete based on the quality of your program, you need to understand the difference between a benefit and a feature of your program. Parents will choose a child care program based on your program's benefits, not its features.

What's the difference between a feature and a benefit?

A feature describes what your program offers.

A benefit tells parents how their needs and their child's needs will be met.

A feature focuses on your program. A benefit focuses on the parent and child.

An example of a feature would be: "My program is licensed." To turn this into a benefit, you would say, "My program meets our state's highest health and safety standards."

Another example of a feature would be: "My program is on the Food Program." To describe this as a benefit, you are better off saying, "I serve nutritious meals that meet federal quality standards to help your child grow."

Take a look at your program's website or advertising flyer and ask yourself the question, "In what way does the description of my program matter to the parent or the child?" If your description doesn't clearly address the needs of your clients, then you've probably written a list of features, not benefits.

Your goal should be to identify three or four key benefits of your program. You should memorize them so you can repeat them to a parent who calls looking for child care.

How can you identify the benefits of your program?

- Think carefully about what it is about your program that helps children learn. Do you have a curriculum that successfully teaches children? Do you provide individualized care and attention that can meet the needs of each child?
- Ask your current clients what they like best about the care you provide.

- Ask the children in your case, “What do you like best about coming here? They are likely to say things like, “I love it when you give me a hug each morning.” “I like playing with the toys.” “I love being with my friends.” Write down whatever they say.
- When parents remove their child from your care, ask them to fill out a parent evaluation form so they can comment on what they liked about your program.
- Ask friends and professional contacts to give you feedback about your program.

You want to come up with one or two benefits that are special or unique. Emphasize the positive aspects of what you do. You don’t need to criticize other programs and how they operate.

All parents want their children to learn and be successful in school. Therefore, make sure that most of your benefits focus on how children learn.

For example, you might say, “Our program offers a child-centered curriculum with planned learning activities.” Or “I rotate a variety of stimulating toys and learning activities throughout the year so children won’t get bored.”

Post your benefits on your website, your business card, your parent handbook, your Facebook page, and in any advertising you do.

It’s a good idea to review your benefits at least once a year to ensure that they are still relevant.

The more you are able to communicate the benefits of your program, the more likely you will be to attract new families and keep them.

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How to Keep Records for Yard Sales and Craigslist Purchases

You're preparing your taxes when you realize that you don't have receipts for a number of items you bought on Craigslist or at yard/garage sales.

Now what?

This is a common concern for family child care providers who often buy such items with cash. But don't give up!

IRS rules say that you must keep adequate records to support the business expenses you claim on your tax return. See IRS Publication 583 Starting a Business and Keeping Records. Ideally, you want a receipt for your purchases, but it's not a requirement.

Here's what you can do when buying items on Craigslist or at yard sales:

- Bring along a receipt book or write down the following information on a piece of paper. It might say: "February 17, 20__ – Used crib – $15 – 1436 Smith Avenue – saw ad on Craigslist." Have the person you bought the item from sign it.
- Save a copy of the Craigslist or yard sale ad you saw in the newspaper or online.
- Take a picture of what you purchased.

If you didn't do any of these things, take the following steps for items you bought in 20__. Write a note describing the date, item purchased, cost, and place of purchase. Estimate the cost if you have to. Take a picture of the items now.

In the future, if you forget to get a signed receipt from the person you bought the item from, try to write down a record of the transaction and take a picture as soon as you can afterwards. It's always a good idea to review your records at the end of each month to catch those transactions where you don't have a receipt.

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How to Keep Track of Your Food Expenses

Keeping good records of your food expenses seems simple enough if you are a family child care provider who uses the standard meal allowance rate.

But many child care providers fail to keep the records they should. As a result, these providers lose hundreds of dollars of business deductions when audited by the IRS. I've seen it happen over and over again.

The IRS standard meal allowance rate allows you to claim your food expenses without having to keep any food receipts! Instead, you must keep the following records: the name of each eligible child, dates and hours of attendance in the family day care, and the type and quantity of meals and snacks served.

If you are on the Food Program, your monthly claim form contains all of this information.

The Problem

The problem is that most child care providers serve meals and snacks that are not reported on their Food Program monthly claim form. This includes meals and snacks served that are beyond the three servings a day per child that can be reimbursed by the Food Program. It can also include meals and snacks that were disallowed by the Food Program.

You are entitled to deduct up to one breakfast, one lunch, one supper and three snacks per day per child, if you serve that many. Meals and snacks served to children that are not reimbursed by the Food Program do not have to be nutritious.

Unfortunately, many child care providers assume that they can claim these "extra" meals and snacks without keeping any records. I hear providers tell me, "It's in my contract that I serve an afternoon snack," or "I always serve an afternoon snack." This is not enough. In an audit the IRS can say, "Since you didn't keep a record during the year, I'm going to deny this afternoon snack."

Losing this deduction can be a big deal. One snack a day served to one child for a year represents over $200 deduction on your tax return.

The IRS rule requires you to keep a daily record of all meals and snacks served. This can be as simple as recording "Sally, Monday afternoon snack," or putting a check mark next to a symbol for a snack each day.

You can track this information if you use the accounting section of the KidKare software program. Or you can use a log found in the annual Redleaf Calendar-Keeper (The log is free online). Or you can use any spreadsheet to track these meals and snacks.

How to Catch Up

If you don't have a daily record showing all the non-reimbursed meals and snacks you served so far this year, what do you do?

Let's say you always serve an afternoon snack. Put each child's name on a piece of paper and use your attendance records to record how many days the child was in your program from the beginning of the year until now. Show your results by month ("January – 22 snacks, February – 20 snacks," etc.).

Ask the parents of each child to sign the bottom of the paper where you have written, "This represents the number of afternoon snacks your child was served in my program from January 1st to _____." If you occasionally served a dinner or took children to a fast food place for lunch, add this to the paper. The parents will know that their child ate these meals and snacks and should be happy to sign it.

From this day forward, keep a daily record of the "extra" meals and snacks served to the day care children. It's okay to go back and reconstruct these records for part of a year, but don't make this a habit. Record these meals and snacks each day going forward. Some Food Program sponsors will allow you to record your "extra" servings on your monthly claim form. Ask them if this is okay before you do so.

The Big Three

The tracking of these meals and snacks is one of the top three things you can do to reduce your taxes. The other two are: keep track of all the hours you work in your home (particularly when children are not present) and save receipts for all expenses associated with your home.

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How to Prepare for an Investigation

by Frank S. Perri, Attorney, CPA

In this article I will examine how a family child care provider can prepare for an investigation.

One of the common characteristics I have encountered with providers who face criminal charges is that they could have avoided being criminally charged if they had properly prepared for an interview they had with an investigator. It is important to be truthful and consistent in your responses to an investigator. It is extremely dangerous to assume that because you believe you are being truthful, the person or persons listening to your version of events will necessarily believe you are telling the truth. If your answers do not appear to make sense, are confusing to understand, or are too inconsistent to be believable, there is a high probability that a provider will face criminal charges.

What providers must do to appear credible and consistent is to practice the answers to questions that an investigator will probably ask them. I have included an accident reminder checklist as a method for a provider to get started in preparing for an interview. Preparation begins the moment you learn of an accident that will probably result in an investigation. By thinking about the questions in the checklist, a provider can focus on the answers she will give. Remember, accidents happen all the time. What gets the provider in trouble is the appearance of lying.

If possible, practice speaking your answers out loud both to yourself and to another person so that you can get some feedback as to how you come across. The questions I have included are not the only questions that you may be asked. It is a good idea to try to anticipate other questions an investigator may ask you.

By properly preparing for an interview, you will gain confidence and reduce your stress. The probability of criminal charges is greatly reduced when you can anticipate the questions being asked and put together a well formulated, consistent response.

Accident Reminder Checklist

- Name of child ______________________________
- Date: _________________________
- What happened to the child (type of injuries, etc.)?
- What actions did you take to help the child?
- When did you first learn of the accident?
- When and how did the accident happen (time, date)?
- Who else was present when the accident happened?
- Did you ask anyone how the accident happened if you did not see it yourself?
- If so, what are their names?

- Where did the accident occur?
- Did you notify the parent(s)? If so, when?
- Whom did you talk to about the accident (names, addresses, telephone numbers)?
- When, where, and how did you talk to others about the accident?
- If hospitalization was required, how long did you wait to go to the hospital from the time that you learned of the accident?
- How long did you wait to call the parent(s) from the time you learned of the accident?
- What actions did you take to make sure that a similar accident would not happen again?

Reminders to Protect Yourself

- Never lie—accidents happen all the time.
- Start filling in the accident reminder check list as soon as possible.
- Remember, an investigator will want details.
- Be consistent in your answers. Inconsistencies will be perceived as a lie even if you are not lying.
- Practice speaking your answers to the accident reminder checklist out loud so that you come across as confident and professional.
- Get honest feedback as to how you appear in your oral presentation when you practice your answers.
- If necessary, get an attorney to help you through the investigation.
- Remember that you are conveying facts, not a story.
- There is no obligation under the law to speak to the police, but you need to be polite and firm and tell them that you do not wish to speak to them and that you want to have an attorney represent you.
- Try to have a witness present when you make the request for an attorney to prevent the police from saying that you never requested an attorney.

Frank Perri has been a criminal defense attorney in Rockford, Illinois, for ten years. He is also a Certified Public Accountant (CPA), prepares tax returns, and represents providers who are audited by the IRS. He has been assisting day care providers for several years since he observed an increase in the number of criminal investigations of providers.

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"Will parents still like me if I charge more?"

That's the fear of some family child care providers who are reluctant to raise their rates.

These providers keep their rates unchanged so they will never have to deal with the stress involved in talking about money with parents.

Others intentionally keep their rates low to assist low-income parents.

However, in my opinion, your goal should be to set your rates so that they will reflect the quality of the care you offer and be competitive with the best programs in your community.

To keep up as the local rates rise with inflation, this means that you will need to raise your rates on a regular basis.

It's true that many providers don't raise their rates for years – but that's exactly how more experienced providers end up earning less than someone who is just starting out.

To make sure that you are being paid according to your years of experience and knowledge, you should consider raising your rates annually. The easiest way to present this to parents is to add a new term to your contract:

"Rates will be raised annually." "Rates will be raised annually in September." "Rates will be raised annually on September 1st by 2%." "Rates will be raised on the child's anniversary date each year, by no more than 3%."

Announcing this new term in your contract well in advance of your next rate increase will put the parents on notice and relieve much of the stress associated with raising your rates. When the time comes, if a parent objects to your rate increase, you can simply refer her to the contract that she signed.

You don't have to give a reason for your annual increase, but if you think it would be helpful, you could explain:

"My expenses (utilities, supplies, training, insurance, food) have gone up this year."

"I have one more year of experience providing child care and I'm using the knowledge I've gained to better help you child learn."

"I have increased the quality of my program over the last year (bought new equipment, attended a training workshop, offered a new curriculum, etc.)."

"I have added more services (longer hours, more flexible pickup time, more field trips, etc.)."

Adding an annual rate increase to your contract doesn't mean that you actually have to raise your rates every year. Let's say that one year you decide not to raise your rates for some reason. In that situation, don't let the date of your annual increase pass without explaining to the parents why you have chosen to skip it that year. You don't want them to think that you have dropped your annual rate increase policy.

You might say, "This year I'm making an exception to my normal policy of raising my rates, since I had to close my program for several weeks due to an illness. However, next year I will follow my contract and raise my rates as usual."

Making it a practice to raise your rates annually will add up over the years. It can make a big difference in your income. If you are charging $180 a week and increase your rates by 3%, that will add up to $5.40 more per week per child. If you work 52 weeks a year, the difference that year will add up to $280.80 ($5.40 x 52 weeks) per child.

If there are five children in your program, you will earn $1,404 more that year. If you raise your rates by another 3% the next year, you will earn an additional $1,446. At the end of two years, you will have earned an extra $2,850.

"Will parents still like you if you charge more?" Who knows? If you really want parents to like you, lower your rates! If your rates reflect the quality of your care, most parents will pay and not complain.

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Most family child care providers understand that they are not saving enough money to meet short-term goals (new car, emergency fund, etc.) or long-term goals (retirement).

The reasons for this are varied: don't have the money to save because of too many bills, a financial crisis (medical bills, credit card debt, parents leaving program), and don't know how to save.

There is no getting around the fact that many family child care providers earn a low income; many make less than minimum wage. Although a very few providers make a profit in their business of more than $40,000, the vast majority of providers are living month to month and have little money saved.

Even so, the most important factor in saving money is not the money you have, but it's rather the will to save. Do you have that will? I think so! As a provider you took the initiative to start a new business on your own and you have patience and perseverance to keep it running. These are the skills needed to save money.

Saving money starts with the understanding that it needs to be a high priority in your life. Saving for retirement, for example, has to be more important than buying a new television or eating out twice a week. If not, you will face a lower standard of living when you do retire.

Start Small

To start a savings plan, start with small steps. It's better to start off with a small savings goal ($25 a month) that you can increase later rather than start with a large goal and find out a short time later you can't keep it up. It's not necessary to set up an ambitious savings plan.

The secret to saving money is to save small amounts on a regular monthly basis over a long period of time. The more time you have until you need your money, the faster it will accumulate each year. This is the result of compound interest. As your savings earns interest in the first year, you will then begin to earn interest on your interest.

For example, if you saved $50 a month and it earned 6% interest, you would have about $618 at the end of the first year. In the second year you would have about $1,255. You earned $55 in interest the second year versus $18 the first year. In the fifth year you are earning about $280 in interest. It can be fun watching this grow!

Compound interest is a powerful long-term savings principle.

If you started investing $3,000 a year at age 35 towards your retirement and you earned 8% a year in an IRA, you would have $339,850 at age 65. But, if you waited one year before you began saving, you would have $311,898 at age 65. In other words, by not saving $3,000 at age 35 you lost almost $28,000 in your retirement account at age 65.

The message is clear. Don't wait to begin your savings plan!

Savings Strategies

Here are some savings strategies to help get you started:

- Identify a particular income stream as your source for savings. Some providers set aside the money they receive from one family as their retirement savings. Other providers use their Food Program check (part or all of it) or late pick-up fees as the money they set aside to meet their savings goal.
- Make direct deposits into a retirement account. Force yourself to save by having money automatically taken out of your checking and put in a savings account dedicated to a short or long-term goal.
- Develop a savings habit by writing a check at the beginning of each month to yourself before you spend money on anything else. If you start to run out of money before the end of the month, cut some expense (eating out, entertainment, etc.) to make ends meet. Don’t spend what you set aside for yourself. Instead, put this into a savings account.
- If you receive any “extra” money during the year, put it into a savings account. Extra money is money that you weren’t planning on receiving before the year began. This can include your tax refund, extra money received from an increase in your rates, an annual increase in the Food Program reimbursement, late pick-up fees from parents, and so on.
- When saving for retirement, make your investments throughout the year rather than at the end of the year. Many providers wait until April to make their retirement contribution for the previous year. Instead, put aside something each month throughout the year. Investing $5,000 a year in equal monthly installments rather than at the end of the year will generate almost $55,000 after 30 years (at 8% interest per year)!

The above strategies are ones that have been used by family child care providers across the country. You can use them as well.

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If you have been in the family child care business for more than two years, is it too late to claim expenses for items you purchased before your business began?

No! Is it too late to claim these expenses even if you have been in business for over 20 years? No!

In this article, we will discuss how to use IRS Form 3115 to recapture previously unclaimed depreciation.

Let's say you started your business in 2008. At that time, you had a house full of items that you started using in your business: furniture, appliances, swing set, fence, toys, silverware, bedding, snow blower, and so on. You probably had hundreds of such items in your home. Once you started using them in your business, you were entitled to start claiming them as business expenses using the rules of depreciation and amortization.

Most family child care providers did not claim these expenses when their businesses began. By not doing so, you lost out on what could have been a substantial deduction that probably would have reduced your taxes.

But it's not too late to recapture these deductions now! Here's how.

First, do an inventory of all items you owned in your home before your business began that you later used in your business. Only include items that you are still using in your business in the current year.

Divide your items into two categories:

Individual items costing/valued at $200 or less

Under the Start-Up Rule, you can deduct up to $5,000 of these items in the first year you used them for your business. Any amount over $5,000 must be amortized over 180 months (15 years).

For example, you began your business in 20__ and your inventory shows you had $9,000 of items individually valued at $200 or less (as of 20__). (Note: The $9,000 represents the value of these items in 20__ multiplied by your Time-Space Percentage) You were allowed to deduct $5,000 of this amount on your tax return, but you didn't.

You can now use IRS Form 3115 and recapture the $5,000 on your current year's tax return. In addition, you were entitled to amortize the remaining $4,000 over 180 months. If you are filing your tax return nine years after your business began, that means you are entitled to claim 9 years' worth of deductions, or 108 months of the 180 months. This is equal to $2,400 ($4,000 divided by 180 months x 108 months = $2,400). Add this amount as well to your Form 3115 for a new total of $7,400. You can continue to deduct $267 ($4,000 divided by 180 months x 12 months = $267) on your 2018 tax return and for the next five years.

Individual items costing/valued at more than $200

You were entitled to depreciate these items when your business began, under the depreciation rules in effect in the year you first started using them for your business. Depreciation rules allowed you to depreciate furniture, appliances and play equipment over 7 years, a fence, patio and driveway over 15 years and a home improvement or home over 39 years. (Note: The depreciation rules change regularly, so check with your tax preparer to find out what rules to apply in that year and after.)

Let's say you owned a $500 refrigerator, an $800 table and a $6,000 fence in 2008 and your Time-Space Percentage was 30% for every year since then. You were entitled to claim $56 on your 2008 tax return for the refrigerator and table, but you didn't. ($500 + $800 = $1,300 x 30% = $390 divided by 7 years = $56*.) But if you use IRS Form 3115 you can recapture all depreciation from 2008 to the current year at once. Because 7 years has passed, you can claim the full $390 of depreciation on this form and deduct it in the current tax year!

You were entitled to claim $120 in depreciation on the fence in 2008, but you didn't: $6,000 x 30% Time-Space % = $1,800 divided by 15 years = $120*.) If you are filing your 2018 taxes, you have 10 years of depreciation to recapture on Form 3115, or $1,200 ($120 x 10 years). In addition, you can deduct another $120 on Form 4562 as the 11th year depreciation deduction.

Note: Many providers failed to start depreciating their home when their business began. You are always better off depreciating your home! You can also use Form 3115 to recapture home depreciation.

What if you bought something after your business began but did not deduct it in the year your bought it?

If the item cost more than $200, you were entitled to depreciate it, so you can use Form 3115 and recapture any unclaimed depreciation from previous years. If it cost less than $200, you could only recapture this deduction back 3 years by amending your tax return.

Summary

Is all of this worth doing? Recapturing depreciation on a $500 refrigerator may not be worth the effort (or cost of having your tax preparer file Form 3115 for one item). But you likely have hundreds of such items, valued at thousands of dollars. Therefore, it is probably worth it!

If you use a tax preparer, present your inventory and tell him/her that you want to take advantage of Form 3115. Let your tax preparer do the calculations.

I have a chapter in my annual Family Child Care Tax Workbook and Organizer on Form 3115 that explains in detail how to fill out this form.

Thanks to Bill Porter for helping me understand these tax rules.

Actually, depreciation is slightly more complicated. You must apply a half year convention in the first year of depreciation, so your deduction would actually be $28 for the refrigerator and table and $60 for the fence. In later years, you would claim the full $56 and $120 and pick up the last $28 and $60 in the last year of depreciation.

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How to Say "No" to a Prospective Client

The moment of truth has come. You need to tell a parent that you don't want her child in your family child care program.

What do you say?

I think the best response is, "I don't think this is the best place for your child at this time."

Or "I don't think my program is a good fit for your child."

Or "I don't think my program can meet the needs of your child."

If the prospective client asks for specific reasons, don't elaborate. If you feel that you must say more, you can add, "It's not personal. I try to make decisions based on what's best for each child, and I have a feeling that your child would be better off in another child care program." The parent can't argue with your intuition.

If you try to give the parent a reason, the parent may feel insulted. She may even think you are discriminating against her if you say the wrong thing.

Unfortunately, many child care providers have trouble following my advice. Some will tell a parent, "I'm waiting to hear from another family who I interviewed earlier this week. If she calls me back, I won't have a space for your child."

There is a problem with this response. What happens if a week later this parent sees an ad you posted on Craigslist or Facebook page? The parent is likely to conclude that you weren't honest with her and feel insulted. She may make a complaint to your licensor. So, I don't recommend doing this.

Some providers will enroll the child for a trial period to see if it will work out. I don't recommend doing this if you have an initial strong feeling that it won't. It will make it even harder to say "no" at the end of the trial period.

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How to Track Hours When Children Aren't Present

Most family child care providers keep relatively good records when tracking the hours when children are in their care. But few providers are keeping accurate records of their work when children are not present.

Want to reduce your taxes? Keep track of the hours you work when children are not present. I can't emphasize this enough. For years I've seen providers pay too much in taxes because they didn't do this.

Now I want to tell you exactly how to record the hours you work in your home when children are not present.

For most providers, tracking the hours children are in their home is relatively easy. You can fill out your Food Program monthly claim form, enter attendance records in your Minute Menu software, or collect sign in/out sheets from parents.

Keeping records of when you are working when children are not in your home is more difficult.

You can count all hours spent on activities that you wouldn't be doing if you weren't a family child care provider. This can include many things: cleaning, activity preparation, meal preparation, talking to parents on the phone, office work, time on the Internet looking for recipes, etc., cleaning toys, reading this blog (!), and so on.

You can't count hours if you are away from home (shopping, training, etc.), even though you may be engaged in a business activity. Only include hours when you are physically at your home and children aren't present. Don't count hours spent on personal activities (mowing the lawn, taking out the garbage, making your own bed when children don't sleep in it), etc.

Before you try to count hours, ask yourself this question: "If I wasn't a family child care provider, would I be doing this activity?" If the answer is "yes," then don't count this time.

How to Keep Records of Hours Worked When Children Aren't Present

You should keep careful records of these hours for at least two months each year. If you can do more than two months, do so.

Because tracking these hours is so important, I want to give a detailed example of exactly how to keep records showing these hours.

First, you want to pick out the two months you will track these hours. Pick two months that are representative of the entire year. Maybe one month in the summer and one month in the fall.

Then start marking on the calendar what the business activity is and the time of day you conduct it.

Tracking Regularly Occurring Activities

There will probably be certain activities that you do on a regular basis, either daily or weekly. Such activities could include: cleaning, office work, meal preparation, or activity preparation. For these activities, write out a description of what you do each time you conduct this activity. For example:

Cleaning

Am cleaning: Monday – Friday: wipe down kitchen counters, sweep kitchen floor, make up beds for napping, vacuum living/dining/playrooms, put away clutter, load dishwasher and run, bring out toys, wash and disinfect toys

Pm cleaning: Monday – Friday: clean off kitchen counters, sweep kitchen floor, do a load of laundry/fold towels & clothes/put away, put dishes into dishwasher, put away toys, clean bathroom, rearrange furniture, vacuum living/dining/playrooms

Sunday: wash kitchen floor, take out garbage, clean first floor windows, sweep front hallway, clean bathrooms, clean up cat litter box, clean children's toys

Office Work

Send/answer emails with parents, pay business bills, record expenses and enter data into Minute Menu software, file paperwork, write newsletters, photo copy forms for parents, communicate with parents on Facebook, place an ad on Craigslist

Meal Preparation

Collect recipes, prepare menus, make up a grocery list, unload groceries, cook/prepare breakfast/lunch

The more detail you can add to your activity description, the better. The purpose of this detailed description is to show why it takes you the amount of time you are recording to do each activity.

I once helped a provider who claimed she spent two hours a day on business cleaning activities. The auditor didn't believe she spent that much time cleaning. But she won her case when she presented the auditor with a full-page description of what she did each day.

Start recording on your calendar when you do these reoccurring activities. For example, you might enter "6-7 am cleaning" on Monday. You don't have to say anything more about what "cleaning" means because you've already written out a full description of what you are doing during this time.

Most providers spend more time on cleaning than any other business activity, so pay close attention to these hours. You can't count all the hours you clean your home because some of these hours represent personal cleaning time. Personal cleaning is the time you normally spend on cleaning up after your family.

So, if you spend one hour on Sunday cleaning (as described above), you wouldn't count the entire hour as a business activity. This is because some of the time is spent on personal cleaning (garbage, cat litter, and part of the time to clean bathrooms that are used by your family and the day care children).

There is no fixed rule to determine how much of the time spent cleaning up after both your family and your business you should count as business time. Make a reasonable guess based on the number of family members and day care children that use the space. Maybe you would record that you spent one hour cleaning on Sunday and count 45 minutes as business time.

I believe it is reasonable to count all the time spent cleaning just before the children arrive and immediately after the children leave. In the end, you need to record some personal cleaning time on your calendar. If you don't, the IRS is likely to assume that some of the business cleaning time you recorded was personal and won't allow you to count it all.

Tracking Irregularly Occurring Activities

Many of the business activities you conduct in your home when children are not present do not occur on a regular basis each day or week. Such activities may include parent interviews, parent phone calls, doing work at home for your family child care association, preparing activities for the children, etc.

Carefully track these activities on your calendar for two months. Be sure to indicate the time of day you do these activities so the IRS can see that you are not doing them when children are present. If you are spending time on activities that need more explanation than the few words you put on the calendar, don't hesitate to write out a detailed note on a separate piece of paper.

Tabulating Your Hours

Assuming that the hours you worked in these two months is fairly typical of the other months in the year, use the average from these months to determine how many hours you spent on these activities for the year.

I've created an example of what your two months of recording hours on your calendar might look like for February and August.

Once you have successfully filled out two months of your calendar with these business activities, add up all of the hours and divide them by the number of days in your two months.

In my example, the provider worked 96 hours in two months divided by 59 days in those two months, equals 1.63 hours per day. Multiply this by 365 days in the year to get 595 hours for the year. Finally, add 595 hours to the total number of hours you cared for children to determine the total number of hours you worked in your home. These hours are recorded on IRS Form 8829 Expenses for Business Use of Your Home, line 5.

(Notice that the provider recorded one hour of cleaning time on Sundays but only counted forty-five minutes as business cleaning. Also, she recorded one hour of personal cleaning time on Saturdays that she did not count.)

Was all this work worth it? 595 hours divided by 8,760 hours (the total number of hours in a year) is equal to 6.8%. That's a lot. This provider could claim 6.8% more of her house expenses (property tax, mortgage interest, utilities, house insurance, house repairs, and house depreciation). If her house expenses are $10,000, she is able to deduct an additional $680.

Another way to look at this is for every 1.5 hours you work cleaning your home, your Time Percent will rise about 1%.

According to a national survey, providers spend about 14 hours per week on business activities when children were not present in their home. (See my book Family Child Care Record Keeping Guide for details)

In Conclusion

I know that most family child providers do not like keeping records. You may even hate just thinking about doing what I describe in this article! But, again and again I see providers who are being audited who have not done this work and they ended up paying more in taxes than they should.

It's up to you.

Tracking the hours, you are doing business activities in your home when children are not present will save you more money on your taxes than almost anything else you can do.

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It can be extremely difficult to get a bank loan to refinance your home or make home improvements. It’s even harder for family child care providers.

Why? Because when banks are determining if a child care provider can afford to pay back a loan, they will look at the child care provider’s profit. This is shown on the bottom line of IRS Form Schedule C Profit or Loss From Business.

Since many child care providers do not make a large profit, they are often turned down for a loan.

Is there anything a child care provider can do to improve her chances of getting a loan to buy, improve, or refinance their home? Yes.

Your Schedule C profit is not an accurate depiction of your ability to pay back a loan. This is because there are a number of expenses on this form that do not represent payments you made that year.

The first type is depreciation. When you buy an item that you depreciate (furniture, appliances, computers, home improvements, etc.), you spread the cost as a business deduction each year over a number of years. The amount of depreciation expenses that are shown on your Schedule C do not represent any actual expense to you for that year.

Therefore, they should not be counted as an expense when applying for a loan. These depreciation expenses appear on Schedule C, line 13. When applying for a loan, the amount on this line should be subtracted from your expenses, which will then increase your profit.

The same logic applies to house depreciation that appears on IRS Form 8829 Expenses For Business Use of Your Home, line 42.

In addition, the remaining house expenses on Form 8829 exist even when you are not in business. They don’t represent costs associated with your business. Therefore, they shouldn’t be included on Schedule C when applying for a loan because they aren’t paid out of your business income. So, you should remove all your house expenses from Schedule C, line 30.

After removing depreciation and house expenses from Schedule C, your profit will be larger and this may make a difference in qualifying for a loan.

Cash Flow Statement

If your bank officer won’t consider your revised Schedule C, your next step is to prepare a monthly cash flow statement. This statement shows the sources of your monthly income and a listing of your monthly expenses. This statement would not include depreciation or non-business expenses (such as your house expenses).

You can download a free cash flow template from my book Family Child Care Business Planning Guide. Click on the tab “Web Components.”

Bank officers are more likely to accept a cash flow statement, although you may still need to explain why this is a better reflection of your ability to pay back a loan than your Schedule C.

Should you reduce your expenses to show a larger profit?

Some providers consider reducing their business expenses to show a larger profit to better qualify for a loan. Is this a good idea?

Maybe. If you can reduce expenses over the next few months to show a higher profit in your monthly cash flow statement, this may be worthwhile to consider.

Before considering this idea check with your loan officer to see if this will matter. Often, they will only want to look at last year's tax return. If this is the case, you may want to consider reducing expenses for the current year to show a higher profit on your tax return. Then reapply for the loan after filing your taxes at the end of the year.

Keeping your expenses low is always a good idea. See if you can find out exactly how much profit you will need to show to be eligible for the loan. Then you can budget your expenses to meet this goal.

One provider wanted to amend her last year's tax return by not claiming $6,000 in food expenses and thus showing $6,000 more in profit. This would only be wise if your loan officer guarantees that you will get the loan. I doubt that he/she will agree to that.

Don't give up if one bank turns you down. Go to the next one. A credit union or neighborhood bank may be more receptive to your loan application than a big bank.

What did you do that made a difference when you applied for a loan?

Tom Copeland – www.tomcopelandblog.com

I Gave a Discount to a Parent. Can I Deduct it?

The short answer is "No."

Family child care providers sometimes offer discounts or scholarships to parents to help them afford their child care services.

For example:

- A provider gives a parent a $100 discount on her services because the parent lost her job.
- A provider gives a parent a $300 scholarship, which by forgives the amount the low-income parent was supposed to pay her as a co-pay.
- A provider gives a parent a reduced fee of $50 for the first week of care as an incentive for the parent to enroll in her program.
- A parent leaves a provider owing her $700. The provider decides not to try to collect from the parent.

In all of these situations, the provider cannot deduct the amounts involved as a business expense.

Instead, the provider will report less income on her taxes and, as a result, pay less in taxes. Only report as income money that you receive. Do not deduct money that was owed to you and not paid or amounts that you offered to reduce your rates as a discount or scholarship.

Note: In general, to deduct a "bad debt," you must have previously included the amount in your income. So, if you entered into your records that a parent paid you $200 when, in fact, she only paid you $100, you could then report the unpaid $100 as a "bad debt." But, since this washes out, the better way to go is to only report as income money you actually receive.

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I Made a Mistake on My Tax Return. Should I Amend It?

Tax season is finally over. Yet, you now realize you made a mistake when filing your taxes. Should you amend your tax return?

As a family child care provider, you shouldn't hesitate to amend your return. Your chances of being audited do not increase when you amend. Don't be shy about amending your tax return! Use IRS Form 1040X Amended U.S. Individual Income Tax Return. You cannot e-file an amended return. I describe how to fill out this form, line-by-line, in my annual Family Child Care Tax Workbook and Organizer.

You should amend your tax return if you forgot to report all of your income, you didn't claim all the hours you worked or all the meals you served or didn't deduct all of your allowable expenses.

For every $100 of business expenses you claim on your amended tax return, you will probably get a refund of between $30 and $40.

Generally, you must amend your return within three years from the date you filed your original tax return or within two years of the date you paid the tax, whichever is later. If you filed your taxes on April 15th of this year, you have until April 15th three years later to amend your tax return.

Additional Rules to Follow

1. Do not amend your return if you made a mathematical error. The IRS will catch this mistake and correct it for you.
2. When filing Form 1040X, attach copies of any schedules that have been affected by your change. In other words, if you are adding additional repair expenses on Schedule C, attach a revised copy of Schedule C Profit or Loss From Business, Form 1040-SE Self Employment Tax, and Form 1040 U.S. Individual Income Tax Return. If you are adding some additional hours, also include Form 8829 Expenses for Business Use of Your Home. Don't resend your original tax forms.
3. If you are amending for more than one tax year, file Form 1040X for each tax year and mail them to the IRS in separate envelopes.
4. If you owe additional taxes, file Form 1040X as soon as possible to minimize interest and penalties.
5. If you are claiming an additional refund, wait until you have received your original tax return before filing Form 1040X. You may cash your original refund check while waiting for the additional refund.

New IRS Tracking System

It normally takes the IRS 8-12 weeks to process an amended tax return. You can check the status of your return online three weeks after you file your amended return. Go to www.irs.gov and search for "Where's My Amended Return." This is also available in Spanish.

State Tax Return

Amending your federal tax return may also require you to amend your state tax return.

Working with Your Tax Professional

If you are amending your tax return because of a mistake made by your tax preparer, you should ask your tax preparer to pay for the cost of amending the return. For example, you gave your tax preparer a list of the number of hours you worked in your home, but he/she did not report them all. If you didn't tell your tax preparer about a new couch you bought, you should expect to pay the cost of amending your return.

It may be that the cost to amend your tax return will be greater than any refund you will receive. If that's the case, don't amend.

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Most family child care providers are not comfortable with choosing investments for their retirement.

Unless you are spending a lot of time researching various investment options, it can be daunting to try and decide what to do with your money.

If you are someone who doesn’t know much about investing, this article offers my simple explanation for what to do to get started. Later you can learn more and make changes to your investments.

When investing for retirement, you want to minimize your risk and maximize your return. To do that you need to have a proper balance of two major kinds of investments – fixed income investments and equities.

Fixed income investments are like IOUs; they include bonds, money market funds and certificates of deposit (CDs). A company or government entity promises to pay you back your investment at a certain date in the future with a fixed rate of return. The interest you earn on these investments are relatively low, but they also have a relatively low risk.

Equities are investments in which you assume some ownership of an asset, such as a company in which you buy shares. These investments include stocks and real estate. Equities have a potential high return and a potential high risk.

- You want some of each type of investment. You don’t want to put all of your money into fixed income assets because your return will be too low to beat inflation.
- You don’t want to put all your money into equities because their value may decline abruptly just at the point when you want to start withdrawing money to live on.

So, what is the best mix of these two types of investments?

Here’s two simple options:

Option #1

60% in the Vanguard Total Stock Market Index Investor Shares Fund

40% in the Vanguard Total Bond Market Index Investor Shares Fund

Option #2

45% in the Vanguard Total Stock Market Index Investor Shares Fund

25% in the Vanguard Total Bond Market Index Investor Shares Fund

10% in the Vanguard REIT Index Investor Shares Fund

20% in the Vanguard Total International Stock Index Fund

Here's why I selected these options. To get the broadest possible exposure to the stock market, invest in a total stock market fund that invests in a representative sample of all companies. You are spreading the risk of equities by buying into the entire stock market.

To get the broadest possible exposure to bonds, invest in a total bond market fund that buys the various types of bonds (short-term, long-term).

Invest in index funds because these have the lowest management fees. The most important factor that will determine the performance of a fund is the annual costs of the fund, according to a study by Standard & Poor's, an investment research and rating firm. This means that the lower the management fees, the higher rate of return you will earn on your investment. The basic conclusions of this study have not been challenged.

Your choice about how much of your money to put into fixed income and equities can be influenced by your age, your willingness to take risks, your health, and other personal circumstances. My suggestions above are a starting point.

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I've Lost My Receipt! Now What?

As we come to the end of the year, it's time for family child care providers to start pulling together their business receipts and other records to get ready for filing taxes.

Keeping good records means having documents that back up your business income and expenses. IRS rules say that you should have an "adequate record" for each expense that you claim on your taxes. The ideal adequate record is a receipt for each purchase.

But what if you don't have a receipt? Maybe you lost it or never received one. What do you do now?

If you don't have receipts, you can still claim expenses on your tax return without them. Other adequate records may include cancelled check, credit or debit card statements, written records you create, calendar notations, and photographs.

All is not lost even if you are missing some of these records at tax time. You can take steps to reconstruct records that will be acceptable to the IRS in an audit. Here are some examples:

If your receipt has faded and is no longer readable, make a photocopy of the receipt or scan it into your computer or phone.

Mileage records – If you don't have receipts to show business trips, review your cancelled checks, credit/debit card statements, training certificates, mileage log, and calendar notations for records of trips. Photographs may show field trips with the children. Bank deposit slips or your check register will show trips to the bank. Use MapQuest or Google Maps to determine the miles to your destinations.

Individual items – Take these steps if you have no records at all for individual items you purchased for your business. Take a picture of each item and write down what you can remember about where you bought it, when you bought it, and how much it cost. If it was purchased new and you know the name of the store, look up the item in the store's online catalog and copy the catalog page.

If you purchased used toys from another child care provider, look up similar items on Craigslist or eBay and copy the page with the advertisement on it. If you paid by check, save the check. Write the notation "toys" on the memo line of the check.

Show a pattern of spending – When you realize that you don't have receipts or other key records, your first step should always be to start keeping better records from that day forward. This can help support your claim for expenses when your records are not complete.

For example, let's say you weren't keeping receipts for cleaning supplies from January – March. If you started keeping receipts in April through the end of the year, you could use your average monthly expenses for the last nine months of the year as an estimate of these expenses for the first three months.

Monthly review – Going forward, conduct a monthly review of your records so you can identify any missing records right away.

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At first glance, these seem like simple transactions between a family child care provider and a parent:

- A parent offers to paint your house, repair your car or install a new deck in exchange for discounted or free child care services
- You offer to give the parent discounted or free child care services in exchange for the parent helping you care for the children

Not so fast.

Whenever you exchange services with parents, it's considered bartering and there are tax consequences that quickly complicate these arrangements.

General bartering rules

You must treat a bartering arrangement as if money exchanged hands. So, let's say a parent painted you house in exchange for you giving the parent two free weeks of child care. If the normal fee for two weeks of care is $300, you would have to report $300 as income because that's what they would have paid you under normal conditions. You could deduct the Time-Space % of the cost of painting the house as a business expense. If you determined that the painting was worth $500 and your Time-Space % was 30%, you could deduct $150.

The parent could claim $300 towards their child care tax credit and would have to report $500 as personal income.

Bartering for child care help

It gets more complicated if you barter with a parent to get their help in caring for children.

Let's say the parent works for you for 40 hours a week for four weeks without pay, and you offer free care for her child for that time. Let's say you would normally pay a helper $8 an hour and your weekly rate for the parent's child is $200.

Parent responsibility: The parent would have to report $1,280 as income ($8 an hour x 40 hours x 4 weeks). The parent could also claim $800 ($200 weekly fee x 4) towards their child care tax credit because that's how much they would have paid if cash had changed hands.

Provider responsibility: The provider must report $800 as income and can deduct $1,280 as a business expense. Since the parent is helping the provider care for children, the provider must treat the parent as an employee. This means the provider must pay the employer and employee share of Social Security/Medicare tax on behalf of the parent. This tax is 15.3% of wages or $195.84. The provider must pay this using the quarterly IRS Form 942. The provider does not have to pay federal unemployment tax because the parent was not paid more than $1,500 in any three months, nor did the parent work twenty or more weeks in the year. In addition, the provider does not have to withhold state and federal income taxes. Check with your state department of labor to see if you have to pay state unemployment tax or purchase workers compensation insurance.

Other issues

If you are going to have a parent work for you, check with your licensor to learn what background checks or training this person must have.

Put your bartering agreement with the parent in writing.

In the above example, you could charge the parent the difference between your regular rate $200 a week and the amount of wages the parent was receiving. Since your rate is $200 a week and the parent is earning $320 per week ($8 an hour x 40 hours), you could require the parent to pay you $120 in cash each week. If you did so, you would also report the $120 as income and the parent could report the $120 towards their child care tax credit.

If you do barter, try not to barter for something that you can't deduct on your taxes. For example, if the parent fixes your car in exchange for free child care, you won't be able to deduct any of the cost of the car repair unless you use the actual expenses method for claiming car expenses. If the parent fixes your motorcycle, you won't be able to deduct anything.

If you agree to barter with one family, you are not required to barter with other families.

Because there is no real tax benefit to bartering, it only makes sense if the parent can't afford to pay you in cash.

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Is There Such a Thing as an Informal Partnership?

Can two people run a family child care business out of a home on an informal basis?

Meaning, can they decide to split the income and expenses and file separate tax forms as self-employed or independent contractors?

I hear about this a lot. The two people may call themselves a partnership or they may say they are running two separate businesses. Sometimes the two people are mother and daughter, or husband and wife, or two friends.

Although an "informal partnership" sounds like a good idea, it's not possible.

The IRS will not accept this. Your options are to operate as a formal partnership (and follow the many rules of a partnership), a sole proprietorship (self-employed) where the owner of the home hires the other person as her employee, a single person Limited Liability Company (LLC) or a corporation. That's it.

There is no such thing as an "informal partnership."

A formal partnership is an unincorporated business run by two or more people who share the profit and loss. What are the consequences of operating as a partnership?

You must file a partnership agreement with your state secretary of state office that spells out the rights and responsibilities of each partner. You can split the income and expenses however you want between you and your partner. Either partner can end the partnership at any time. Each partner is legally liable for the actions of the other partner.

You and your partner must file partnership tax forms and there are no tax savings over a sole proprietor. In fact, you will lose some of your house expense deductions if you form a partnership. The partnership would have to pay rent to the owner of the home and the owner would report the rent as income on Schedule E. Not all house expenses can be deducted on Schedule E (house depreciation being the major one).

The record keeping rules for a partnership are more complex than a sole proprietor as you must keep your business and personal expenses completely separate. Any items that the partnership purchases are the property of the business, not the partners individually. This requirement is particularly difficult to meet because providers buy so many items that are used by their business and their family.

As you can see, there aren't really many benefits of forming a partnership other than making each person responsible for the business. Forming a partnership with your husband makes no sense. Have him work for free or hire him as an employee.

There are many complex tax and legal issues when deciding to operate your business other than as a sole proprietorship (another name for self-employed). I strongly recommend providers consult with a tax preparer and lawyer before taking this step.

What's a better alternative than a formal partnership?

The best option is to be a sole proprietor and hire your friend to be your employee. The person who owns the house where the child care is offered should always be the employer so they can continue to deduct all house-related expenses.

I've written about the pros and cons these business structures at length in my book Family Child Care Legal & Insurance Guide.

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Have you recently conducted a household inventory where you have listed and photographed every item in your home?

There are two reasons why every family child care provider should do so.

First, there are thousands of dollars’ worth of tax deductions sitting in your family child care home, waiting for you to report them on your tax return.

Second, your inventory will be extremely valuable when making an insurance claim if your property is ever damaged or destroyed in a fire, tornado, hurricane, flood, or if your home is burglarized.

The picture above is of a family child care provider’s kitchen damaged by a grease fire.

Business Deductions

You are entitled to deduct household items you use in your business.

Such household items include your washer, dryer, refrigerator, stove, television, beds, tables, chairs, lawn mower and snow blower. In addition to furniture and appliances, you can also include rugs, lamps, bedding, silverware, pots and pans, curtains, towels, tools, and so on.

Anything that you owned before you went into business that is now being used in your business can be claimed as a business expense. In addition, you can deduct the business portion of anything purchased after your business began, with the exception of a house, home improvement and home addition.

Conduct an inventory of all household items by writing them down. This job can be made easier by using my Family Child Care Inventory-Keeper. It is an easy-to-use log that enables you to track your household items by room.

Since you probably don’t have receipts for these items, take pictures to support your deduction.

Take enough pictures in each room so that you can identify individual items.

Estimate each item’s value as of the day you first started using it in your business. Use thrift store or garage sale prices. You don’t need a receipt to depreciate these items.

This may seem like a lot of work, but it is well worth your time.

Let’s say you started your business this year and the value of all your household items was $10,000. If your Time-Space Percentage was 40%, you can deduct up to $5,000 of such expenses this year. Since $4,000 ($10,000 x 40%) is less than $5,000, you can deduct the entire amount this year.

If you started your business more than two years ago and didn’t claim these expenses, you can file IRS Form 3115 and claim the $4,000 on this year’s tax return as long as you still own and used the items in your business this year.

Many child care providers fail to take advantage of the tax rules that allow you to deduct household items they owned before their business began. Turn over your inventory list to your tax preparer and have him/her calculate this deduction. If you do your own taxes, use my annual Family Child Care Tax Workbook and Organizer to calculate your deduction.

Insurance Protection

You want a photographic record of everything in your home so that you can make a claim for damage or loss with your insurance company.

Take pictures of everything in each room in your home (including your basement and garage). Open desk and dresser drawers, kitchen cabinets and take pictures of everything inside (particularly of valuable items such as jewelry). Take pictures of your closets, your backyard (patio chairs, grill, swing sets, etc.), and your laundry room.

Put these pictures on a flash drive and put them in a safe deposit box. (The cost of the flash drive and part of the cost of the safe deposit box can be a business expense!)

Conclusion

You’ve probably heard before the importance of conducting an inventory of household items and taking pictures of everything in your home. You know you should do it. Make this year the year you do!

Tom Copeland – www.tomcopelandblog.com

How can providers protect themselves in these situations?

- A parent threatens to turn a provider into child protection (claiming she abused her child) unless the provider drops her demand to be paid for a two-week notice.
- A parent calls a provider's licensor to falsely complain that her provider left her child alone while the provider went shopping.

There is no way a provider can prevent a parent from making a false complaint to child protection or licensing. Here are some steps that all providers can take to help reduce the consequences of such complaints:

1. Purchase business liability insurance that covers accusations of child abuse against you and all members of your family as well as any employees you may have. Once you are accused of child abuse, you should immediately contact your liability insurance agent and ask for guidance.
2. Keep in close communication with your licensor about any potential problems with parents. Licensing workers say that if they know there is a conflict between the parent and the provider about payments before the parent calls and makes a child abuse allegation, they are much less likely to take what the parent says seriously. This can make a big difference when it's one person's word against another.

Therefore, you should call your licensor to report parent problems as they occur. The purpose of these calls to your licensor is not to ask for help in resolving the conflict, but rather to go on record as saying that a conflict exists. This will help support your position later that the parent is making up the accusation to avoid paying what he or she owes you. Some of the best times to call your licensor are when you are about to terminate a parent, when a parent terminates care, when you are about to send a letter to a parent demanding payment, and when the parent threatens you with making a complaint.

3. Keep careful chronological notes of the conflict you are having with parents. Write down what the parent says to you if they are complaining about your care. You want to be able to remember exactly what the parent said so that it can be compared to what they tell licensing.
4. Lastly, require parents to pay you at least a week in advance and pay you for their last two weeks of care in advance. If you follow these rules, a parent will never leave owing you money. Therefore, you won't have to threaten parents with a lawsuit to collect what they owe you, and parents will be less likely to make false accusations to avoid paying.

None of these steps will guarantee that you won't be faced with a child abuse investigation. Unfortunately, providers are vulnerable to vindictive parents. If you have experienced such false complaints and came out of it without penalty, you may want to consider talking to your local media about your story. The more the public understands that false accusations do occur, the more likely it is that the next falsely accused provider will get better treatment.

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Questions Your Tax Preparer Must Answer Correctly

It can be a challenge finding a tax professional who understands your family child care business. This is because there are a number of unique rules affecting child care providers.

To make sure your tax professional is familiar with your business, here are some key questions to ask:

Should I depreciate my home? – *Answer: Always yes! No matter what.*

Can I count the hours I spend cleaning my home, preparing activities and meals, using the Internet, and record keeping for my business after the children are gone? – *Answer: Yes! These hours will make a big difference in increasing your Time-Space Percentage.*

Can I depreciate the furniture and appliances that I owned before I went into business? – *Answer: Yes! Claiming this depreciation will help reduce your taxes.*

If have never claimed this depreciation, is it too late to claim it now? *No! You can file IRS Form 3115 and recapture this depreciation as far back as you have been in business. I've talked with child care providers who deducted thousands of dollars of past depreciation on their home, furniture and appliances.*

Can I deduct meals that are not nutritious and not reimbursed by the Food Program? – *Answer: Yes!*

May I deduct household items such as cleaning supplies, light bulbs, lawn mower, rugs, pots and pans, couch, bed that children sleep on, doorbell, new window, etc.? – *Answer: Yes! You are entitled to deduct all "ordinary and necessary" expenses associated with operating a home learning environment for children.*

Can I have an exclusive business room and other regular use rooms when calculating my Time-Space %? – *Answer: Yes!*

If I have a substitute who helps me care for children for six days this year, do I treat her as an employee or an independent contractor? – *Answer: Employee! Unless this person is self-employed as a substitute caregiver who works for other providers, you must pay payroll taxes (Social Security tax, unemployment tax) regardless of how few hours she worked or how little you paid her.*

If the person you are considering doing your taxes cannot answer these questions correctly, and insists that the above answers are wrong, you should seriously consider finding someone else to do your taxes.

My book, Family Child Care Tax Companion is designed for providers who use tax preparers. Give a copy to your tax preparer to ensure he/she is not making major mistakes on your tax return.

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Emergencies can cause injuries, property damage, and emotional trauma. They can also take a financial toll. Here are five steps you can take to plan ahead so you recover as quickly as possible.

1. Establish an Emergency Fund

Emergencies are always unexpected. And they come with a cost. Therefore, it makes sense to save some money ahead of time to cover expenses associated with emergencies. You want to be able to pay for any insurance deductibles on your homeowner's and automobile insurance policies. You also want to have enough money to tide you over if you are forced to shut down your business for an extended period of time.

Start by establishing an emergency fund. Ideally, you want enough money in your fund to cover all insurance deductibles, plus basic living expenses for at least three months.

You probably don't have enough money now to fully fund your emergency fund. That's okay! Get started now by setting aside a small amount of money each month that will build up over time. Some family child care providers dedicate certain sources of money for their emergency fund. It can be a portion of your Child and Adult Care Food Program (CACFP) monthly reimbursement, parent registration fees, or late payment fees. Any tax refunds, or other unexpected money you receive throughout the year, can also be added to this fund.

Put your emergency fund money in a separate account and don't touch it for any reason other than responding to an emergency. Because you'll need access to it in a hurry, don't invest this money in the stock market where it could lose its value, or in CDs where there is usually a penalty for early withdrawal. Instead, put it in a checking or savings account or a money market fund where there is little or no risk, but will allow you immediate access to the funds.

Small amounts of money add up. If you put aside $50 a month, you'll have $600 by the end of the year and $3,000 in five years.

2. Conduct a Household Inventory

If your business or personal property is damaged or destroyed in a natural disaster or is lost due to vandalism or theft, you expect your insurance to pay for the cost of repairing or replacing your items. (Check with your homeowners' insurance agent to make sure your policy covers all items in your home that are used for your business, including your furniture and appliances.) But, insurance won't pay for items if you can't identify what was lost, destroyed, or damaged.

Therefore, you want to conduct an inventory of all your household items, business and personal, so you can make an accurate insurance claim. You will need to record a description of the items and their value. You should consider making a photographic record of everything in your home. Take pictures (or a video) of everything in each room, including your basement and garage. Open desk and dresser drawers and kitchen cabinets to take pictures of everything inside (particularly of valuable items such as jewelry). Take pictures of the inside of your closets, your backyard (patio chairs, grill, swing sets, etc.), and your laundry room. As you buy new items, take a picture of them. Put these pictures on a flash drive and put them in a safe deposit box. (The cost of the flash drive and part of the cost of the safe deposit box can be deducted as a business expense!)

There are also tax advantages of conducting an inventory. You are entitled to depreciate the value of all your household items at the time you first started using them in your business. If you have been in business for a number of years and haven't taken this depreciation, it's not too late to do an inventory. You can use IRS Form 3115 and recapture all previously unclaimed depreciation going back to your first year in business.

3. Keep Business Records in a Safe Place

Keeping good business records is a difficult task for most family child care providers. To ensure that your hard work doesn't go to waste, make sure you are storing the records in a safe place so they are not lost as a result of a natural disaster or fire. For tax purposes, you should save all your business receipts and records for at least three years. Save your tax returns for as long as you live.

Put your business records in plastic containers (to protect them from water damage), or better yet, put them in a fire-resistant file cabinet. An increasing number of providers are scanning their receipts and records onto their computer. If you do this, download these files onto a flash drive and put them in a bank safe deposit box to ensure their preservation. IRS rules say that you don't need to save paper copies of receipts if you scan them into a computer. You can save personal records (birth certificates, passports, wills, valuables, etc.) in a safe deposit box.

4. Identify a Backup Caregiver

After an emergency, you may need a backup caregiver to watch the children in your care for a short or long period of time. This can happen if you are physically injured or if your home is damaged.

Plan ahead and identify a backup person now. Start your search for a backup caregiver by contacting your local child care resource and referral (CCR&R) agency. They may be able to identify persons for you. Talk to your child care licensor who can tell you what qualifications this person must have.

You may want to line up several persons to be your backup to ensure that someone will be available after an emergency. Also, it's important to find out whether your commercial business liability insurance policy covers you if you are operating outside of your home, or if someone else is temporarily caring for the children.

Note: In most cases, your backup caregiver will need to be covered by workers' compensation at the time they start caring for children. Since you won't know when an emergency will happen, it's important to get this insurance now. It's unlikely that you will need this insurance if you don't pay the person for their work but check with the state workers' compensation office to be sure. The cost of workers' compensation insurance is modest, and you may get a partial refund of the cost if you don't pay anyone by the end of the year.

Having a backup caregiver will reduce stress for the children in your care and your daycare parents after an emergency. It will also increase the chances that they will come back to your program once you are able to restart your business.

5. Set Policies on Parent and Staff Payments

If you have an emergency and must close your business for a day, a week, or a month, are parents required to pay you during this time? If you have paid employees, will you pay them if you are closed after an emergency?

These are questions you want to answer before the emergency happens. If you haven't previously addressed these questions, you may face unnecessary stress in deciding what to do when an emergency arises. You can set whatever policies you want to answer these two questions. Most providers put in their contract that parents must pay for short-term closures such as a provider illness, vacation, holiday, personal days, funeral days, etc.

You should consider adding natural disasters and other emergencies to the list of days that parents have to pay if you are closed. Requiring parents to pay for up to a week or so of closure is reasonable. You are also free to make your own decision about whether to pay helpers if you are closed because of an emergency. You are not required by law to pay staff for days you are closed. You may not want to put this in writing to give yourself maximum flexibility in dealing with emergencies. Paying salaries for one or two days may not be a big deal, but these costs can add up quickly and you don't want to commit yourself to this unless you have the necessary resources (perhaps in your emergency fund).

Summary

Emergencies will almost always cost you money that you didn't plan on spending when the year began. You can reduce the financial pain of an emergency if you follow these five steps and plan ahead.

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I’ve been talking to family child care providers for many years about the importance of claiming all allowable deductions for your business. Doing so will reduce your taxes.

But does this mean you should spend more money just to increase your deductions?

The answer is no! You are always better off financially if you save your money rather than spend it.

Don’t follow this logic: “Last year I spent $800 on toys and supplies, and I’ve only spent $500 so far this year. I need to go out and buy more toys so I can reduce my taxes.”

Let’s say you had $500 in your wallet. You have two choices. First, you could spend the $500 on toys and deduct the full amount on your taxes. If you do this, you will reduce your taxes by about 30% of this amount (federal and state income tax, plus Social Security tax). So, you would reduce your taxes by $150. At the end of the year, you spent $500 and got back $150. You now have $150 in your wallet.

What if you decided not to spend the $500? You would pay tax on a higher profit of $500 and owe $150 in taxes. But you would have $350 left in your wallet!

Your goal should not be to lower your taxes, but to have more money after your taxes are paid. After all, if a parent offered you an extra $20 a week, you would accept the money even though doing so would increase your taxes.

If you spend money for your business, do so because your need it for your business. Don’t spend money just so you can claim a deduction. Keeping your expenses low does pay off.

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Setting Financial Goals for the New Year

As we close out the year, let's pause to count our blessings with family and friends.

As we think about the coming year, I recommend that you consider setting some financial goals for yourself and your family.

Most of us spend more time planning our next vacation than we do planning our financial future. But, unless we do set goals, it will be unlikely that we will make much progress in improving our financial situation.

So, start the new year by identifying several financial goals you would like to achieve by the end of the year. They can be short or long-term goals, or a combination of both.

Because it can be hard to take the first step, here are some suggestions. Your financial goals may be different.

1. **Capture the employer match for retirement contributions**

   If your spouse has a 401(k) or 403(b) IRA plan at work, make sure he contributes enough so he or she receives the maximum employer matching contribution. This is free money and should be at the top of your list of priorities for the year.

2. **Gain more control over your expenses**

   Seek to reduce or eliminate your credit card debt. If you can't pay off your credit card in full at the end of each month, this is a sign of over-spending. If you have an unpaid balance, start by paying off any new spending each month. If you can't pay off this debt in one year, try to reduce it by half or a third.

3. **Establish a three-month emergency fund**

   Life is full of unknowns, so set up an emergency fund to cover the unexpected (house repair, medical bill, loss of a family, etc.). You may want to start by setting a smaller goal of a one-month emergency fund for the first year.

4. **Set up a car replacement fund**

   Borrowing money to buy a car means you are paying interest for something that is decreasing in value over time. Ideally, you should pay cash for your next car. If this isn't possible, start saving for your next car so you can increase your down payment substantially.

5. **Save at least 10% of your profit for your retirement**

   The sooner you start saving for your retirement, the better. 10% is a reasonable goal if you are in your twenties or thirties. If you are older, saving 20% should be your goal.

These five financial goals may be very different than the ones that make sense for you. You may only want to set one or two goals this year.

Once you set your goals, monitor them throughout the year. At the end of the year, measure how well you have done and then set new goals for the next year.

Don't be discouraged. Don't worry if you don't meet all of your goals for the coming year. It's more important to regularly set goals and mark your progress. Doing so will make it much more likely you will meet them.

Taking small steps now will make a big difference in the long run.

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Should You Be on the Food Program?

Some family child care providers continue to question whether it's worthwhile or not for them to join or stay on the Food Program.

It's always financially beneficial for you to be on the Food Program!

Here are some frequently asked questions from providers who question this.

Question: My tax professional says I'm better off not on the Food Program because my taxes are now lower. Is this good advice?

Answer: No! Reimbursements you receive from the Food Program are taxable income. (The only exception to this rule is any reimbursements you receive for your own children are not taxable.)

Some people think that this is a reason not to be on the Food Program. Wrong!

Let's look at an example: Natasha Provider is not on the Food Program, earns $30,000 from parents and spends $5,000 on food. She can deduct the $5,000. She then joins the Food Program and receives $4,000 in reimbursements from the Food Program. She now reports $34,000 in income and the same $5,000 in food expenses.

You don't lose your ability to claim the same amount in food expenses just because you join the Food Program!

So, her income is now $4,000 higher, meaning she will pay more in taxes because of this extra income. If she is in a high tax bracket of 32% (12% federal income tax, 15% Social Security tax, and 5% state income tax), she will owe an additional $1,280 in taxes.

Is paying more in taxes a reason to refuse to join or quit the Food Program? No. Natasha has an extra $2,720 in her pocket, after taxes ($4,000 income – $1,280 taxes = $2,720).

So, even though Food Program reimbursements are taxable income, you are still better off financially after joining.

Won't I lose the ability to claim my food expenses if I join the Food Program?

No! Your food deduction will be the same, whether you are on the Food Program or not. When you join the Food Program, you can deduct the meals and snacks you are reimbursed for as well as the ones you are not reimbursed for.

I was on Tier II and the reimbursements I received from the Food Program did not cover the cost of the food, so it was not worth it.

Wrong! Food Program reimbursements were not designed to cover all of the cost of the food you serve. Some money is always better than no money. If you served one breakfast, one lunch and one snack each day and are on the lower Tier II rate, you would be receiving $595 per child per year. That's better than a kick in the head. Take the money.

Is it really worth doing all that paperwork for a 21-cent snack (current Tier II rate)?

Yes! A typical provider will earn over $10.04 per hour by claiming this snack. If you served one snack a day and cared for four children, you would receive $218 a year ($.21/day x 5 days a week x 52 weeks a year x 4 children). If it takes you five minutes a day to claim this snack, you will earn $10.04 per hour for your work (5 minutes a day x 5 days a week x 52 weeks = 21.7 hours divided by $218 = $10.04)

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Should You Buy or Lease a Vehicle?

The answer is clear: if you want to spend less money on transportation over the long run, buy a vehicle rather than lease one.

So why do some family child care providers lease?

Leasing upfront costs are lower and leases have lower monthly payments than if you buy a vehicle. This makes leasing attractive because it allows you to drive a more expensive vehicle than you might otherwise be able to afford if you are buying.

I understand the lure of driving a fancy vehicle; television ads make it sound like it's un-American not to have one. These ads focus on how little you can pay each month to lease. However, you should not base your decision to buy or lease on the amount of the monthly payment. Instead, look to the actual cost of your vehicle over time. In the long run, leasing will always cost more.

The fact that you can deduct the business portion of the cost of your vehicle lease does not make leasing less expensive than buying. Spending more to get a larger business deduction will reduce your taxes but will leave you with less money in the end. For example, if you spent $1,000 more each year to lease rather than own a vehicle, and you were able to reduce your taxes by $300, you would still have $700 less than if you hadn't spent the money in the first place. In other words, giving $1,000 to the vehicle company so you can get $300 from the IRS doesn't make financial sense.

So, when you see others driving fancy vehicles down the road, remember that they are probably spending more than you. Use the money you saved by buying your vehicle for more important things in life.

If you do decide to lease, you have the same choice in how to claim vehicle expenses as if you bought a vehicle; use the standard mileage rate or the actual expenses method.

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Should You Depreciate Your Home?

Yes! Always! No exceptions!

Unfortunately, some family child care providers are told by their tax preparer not to depreciate their home on their tax return (Form 8829 Expenses for Business Use of Your Home). You will be making a big mistake if you listen to anyone who tells you this.

Why? Two reasons.

Reason #1: Claiming depreciation on your home represents a big deduction and lower taxes for you. Home depreciation is based on the purchase price of your home (in most instances). Let's say you bought your home for $100,000 and your Time-Space Percentage is 40%. The business portion of your home is $40,000 ($100,00 x 40%) that would depreciate over 39 years. The represents about a $1,000 business deduction each year ($40,000 divided by 39 years). Not bad!

Reason #2: When you sell your home you face two possible taxes. The first is capital gains tax on the profit on the sale of your home. You can avoid this tax on the first $250,000 of profit if you are single or $500,000 profit if you are married. Nice! Most child care providers can avoid worrying about this tax.

The second tax is tax on the house depreciation that you claimed while using your home for business. This tax is unavoidable and must be paid when you sell your home. The amount of tax you will owe will depend on your family's tax bracket at the time. The tax rate will be either 15% or 25%. Let's say you were in business for six years and claimed $1,000 in depreciation each year. Then you go out of business and five years later you sell your home. You will owe tax on $6,000 and will pay either $900 or $1,500.

What if you don't depreciate your home?

You will still owe $900 or $1,500 in taxes!

That's because the IRS rules clearly state that if you are entitled to claim the depreciation deduction on your home, you will be treated as if you did when you sell it. If house depreciation is "allowed or allowable", you must pay tax on it when you sell your home. The only situation where a provider would not be "allowed" to claim house depreciation is if they have a business loss.

Therefore – always depreciate your home, no matter what! You will owe the same tax later even if you didn't depreciate it and you will have lost a lot of deductions.

If you have not depreciated your home in the last three years, amend your tax return (Form 1040X) and get a refund.

If you have not depreciated your home for more than three years, use IRS Form 3115 to recapture all previously unclaimed depreciation on your current tax return.

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At the time it sounded like a good idea. You and a friend decided to care for children together in your home and split the income and expenses. You called yourself a partnership, but you didn't write up a partnership agreement.

To keep things simple, you decided that you will claim your house expenses on your tax return and your friend will report her income and some business expenses as an independent contractor on her IRS Form Schedule C.

I have heard about this situation from family child care providers across the country. Sometimes the partners are mother and daughter or husband and wife.

Unfortunately, you can't operate your business in this fashion.

You must either structure your business as a partnership (and follow the rules of a partnership), a sole proprietorship (self-employed), a single person Limited Liability Company (LLC) or a corporation. That's it. If you try to run your business as an informal partnership as described above, you will run into trouble with the IRS. In addition, if a child is injured, you can both be sued.

A partnership is an unincorporated business run by two or more people who share the profit and loss. What are the consequences of operating as a partnership?

You must file a partnership agreement with your secretary of state office that spells out the rights and responsibilities of each partner. You can split the income and expenses however you want between you and your partner. Either partner can end the partnership at any time. Each partner is legally liable for the actions of the other partner.

You and your partner must file partnership tax forms and there are no tax savings as compared to a sole proprietor. The record keeping rules for a partnership are more complex than a sole proprietor as you must keep your business and personal expenses completely separate. Any items that the partnership purchases are the property of the business, not the partners individually.

As you can see, there aren't really many benefits of forming a partnership other than making each person responsible for the business. Forming a partnership with your husband makes no sense. Have him work for free or hire him as an employee.

What's a better alternative than a partnership?

You can be a sole proprietor and hire your friend to be your employee. The person who owns the house where the child care is offered should always be the employer so they can continue to deduct all house-related expenses.

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Should You Form an S or C Corporation?

The answer is: Do not do this unless you have consulted with an attorney and a tax professional and know exactly what you are getting yourself into. Forming an S or C Corporation makes sense only for a very small number of family child care providers.

An S or C Corporation is the most complex business entity under which to operate your child care program. When forming either of these types of corporations you must follow your state requirements that usually include identifying corporate officers, drafting articles of incorporation and bylaws, and holding stockholders meetings. This is a lot of additional paperwork.

These corporations must pay state filing fees, annual state business fees, and higher tax preparation fees.

The main advantage of these corporations is reduced personal liability. This means that you are no longer personally liable for the debts of the business and in a lawsuit; only your business assets would be at risk. However, you can still be sued personally if you are negligent (shaking a baby or child abuse). Incorporating is no substitute for purchasing a lot of business liability insurance coverage ($1 million per occurrence and $3 million aggregate).

It's possible to reduce your federal taxes by incorporating as an S or C Corporation. You will have to set yourself up as an employee of the corporation and pay various federal and state payroll taxes. But you can reduce your Social Security taxes by distributing some of your profit as dividends rather than as salary. There are differences in the taxes paid by an S or C Corporation. You will be better off with an S corporation if your profit is smaller.

This tax benefit comes at a price: You will owe federal and state unemployment taxes, file numerous federal and state payroll tax forms, and file quarterly estimated taxes. Your state may also require you to purchase workers compensation insurance.

Another drawback to being a corporation (other than the additional record keeping and paperwork) is that you lose the ability to deduct house depreciation. This can be a major loss of a business deduction. It can be overcome but only if your profit is high enough (perhaps more than $30,000 per year).

This is only a brief summary of S and C Corporations. You should learn much more about these entities before making a decision to incorporate.

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It's a necessity for most businesses to have a business checkbook where the owner deposits her income and pays business expenses.

But family child care is a unique business in that most expenses are both business and personal (toilet paper, cleaning supplies, furniture, appliances, and so on).

When you write a check for such items do you write it out of a personal checkbook or business checkbook?

Do you need a business checkbook?

It's up to you.

You are not required to have a business checking account.

Child care providers are divided on whether or not they find a business checkbook useful. Some believe it is a sign of professionalism. Some use a business account to deposit all their income. Others use this account for expenses that are exclusively business, such as payroll for employees, equipment, toys, and so on.

You can run your business income and expenses through one personal account. Many child care providers have done so for years without problems. You can write checks for business expenses out of either a personal or business account. It doesn't matter. If you get audited by the IRS, they will look at both your business and personal checking accounts.

Before you open a business checking account, you should find out if the fees are higher than a personal account. Sometimes having two personal accounts will be cheaper than one of each.

If you have a business name and parents are writing checks to your business name, you will probably need a separate business account. Check with your bank.

Some child care providers open a separate business savings account. One child care provider deposits her fundraising income into this account. Others put aside money for special purchases, such as an outdoor climber, or save it for a rainy day.

I have also talked with child care providers who have a separate business credit card.

If you always purchase items for your business with a check, credit card, or debit card, you will have a paper record that will make claiming business deductions on your tax return easier. You will also have an easier time defending your expenses if you are audited.

If you pay by check, be sure to also keep a receipt to show what you bought. If you don't have the receipt, make a note in the memo line of the check about what you bought ("toys," "children's supplies," etc.).

When you must use cash (garage sales, Craigslist, etc.), write down your purchase on a piece of paper. Then take a picture of your purchase.

Note: If you incorporate your business or form a partnership, you must keep a separate business checking account. You cannot co-mingle business and personal funds. That means you must write a check out of your personal account for all expenses that are both business and personal. If you fail to do so, you will likely lose you the protection that incorporation normally brings.

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Should You Hire Your Child Who is Age 18+ or Your Husband?

The simple answer for a family child care provider is – only in a few unique situations.

If you pay your own child who is age 18 or older or if you pay your husband to do work for your business, you must treat them as your employee.

This means withholding Social Security/Medicare taxes and withholding federal and state income taxes. If your child or husband is over age 21, you must also pay federal unemployment tax. Although you can deduct these taxes as a business expense, your child or spouse must report their earnings as income on their IRS Form 1040. Therefore, there is little tax advantage to paying them.

If you do hire your own child or spouse, you must also keep specific records and file a series of tax forms. The IRS requires you to file Form 941 quarterly or Form 944 annually, Form W-2 and Form W-3.

The rules are quite different if you hire your own child who is under age 18. In that case you would not have to withhold Social Security/Medicare taxes or pay federal unemployment taxes.

A warning: Check with your state workers' compensation office to see if you must purchase workers' compensation insurance when hiring family members. Most states do not require this. However, in some states (New York being one that I know of), you must purchase workers' compensation insurance for anyone who is with you when caring for children. This includes volunteers and family members (even if you don't pay them!).

Reasons to Hire

There are a few situations where you may want to consider hiring your own children or your spouse:

- You want your children to learn the value of work and understand how to manage their own money.
- You want your children or spouse to earn wages to increase their lifetime Social Security benefits. The more they earn, the more they will receive from Social Security.
- Your family has at least $1,000 of medical expenses that are not covered by insurance (this includes medical insurance premiums your husband pays at work). If you are in this situation, you can establish a medical reimbursement plan (a Section 105 plan) that allows you to deduct 100% of all your uninsured medical expenses as a business deduction.

Simple Solution

If your children or your spouse are working for you, you are not required to pay them! However, be sure to check with your state workers' compensation office to see if you must purchase insurance when they are helping you care for children, even if you aren't paying them as an employee.

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For the vast majority of family child care providers, the answer is "no".

However, I continue to hear from family child care providers that they have been advised by their tax professional or a lawyer to incorporate their business.

Some have incorporated without understanding the consequences of their action.

Types of Business Structures

There are four basic types of business structures under which you can operate your business: sole proprietor (also known as self-employed), partnership, a single person Limited Liability Company (LLC), and a corporation (S or C corporation).

Once you start your business, you are automatically treated as a sole proprietor. There are no forms to fill out. If you are going to consider operating under one of the other three options you should know that this can be a very complicated decision with both tax and legal complications. Therefore, before making this decision I strongly recommend that you consult with both a tax professional and an attorney who understand family child care.

There are two basic reasons why child care providers consider other business structures: lower taxes and personal liability protection.

Taxes

There are no tax savings if you form a partnership or single person LLC. There may be some tax savings if you operate as a corporation, but probably only if you have a profit of at least $30,000 each year. Also, take these points into consideration: you will lose the ability to deduct your house depreciation if you form a partnership or S or C corporation, the cost to set up a corporation can be hundreds of dollars, there are annual fees for corporations and LLCs, and your tax preparer will probably charge you more to do corporate tax returns. Ask your tax preparer to show you exactly how much in taxes, if any, you would save by incorporating.

Personal Liability

If you form an LLC or incorporate your business, you may get some personal liability protection. This means that your personal assets may be protected if you are sued. However, you should not assume that such protection is automatic. If you are negligent and a child is injured or if you are accused of child abuse – being incorporated won't protect you. In addition, there are many business formalities to follow as a corporation (separate business and personal records, stockholder meetings, following your bylaws, etc.) and if you fail to follow them all you could lose this protection.

The biggest problem of being a corporation (including an LLC) is the extra record keeping. You must keep separate business and personal records. Let's say you go to the store and buy some paper towels and laundry detergent. Since this is both a business and personal expense, if you write a check from your business account (or from your business credit card) you have commingled business and personal funds and you will lose any personal liability protection.

So, you must pay for items that are both business and personal out of your personal account. You can deduct the business portion of the paper towels and laundry detergent by applying your Time-Space Percentage. But you won't know your Time-Space Percentage until the year is over. At that time you would write a check out of your personal account to your business account for each such receipt. What a pain in the neck!

Summary

Forming an LLC or a corporation is no substitute for having an adequate amount of business liability insurance ($1 million per occurrence and $2-3 million aggregate). With this insurance, you can adequately protect yourself from risks associated with your business.

Child care providers who have a large business profit each year (at least $30,000), have a significant amount of personal assets they wish to protect, don't mind doing extra record keeping, and plan to be in business for a number of years may want to look into a business structure other than a sole proprietor. You should seek out professional legal and tax assistance before you incorporate.

Everyone else should keep operating as a sole proprietor.

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A family child care provider tells me she paid herself $20 a week to clean her home. She then deducted this as a business expense.

Another provider asks if she can pay herself a salary.

Neither is allowed.

If you are self-employed, you can't pay yourself for doing work for your business.

You can't pay yourself a salary for working for yourself.

You are entitled to all the money that you don't spend on your business.* You can simply take money out of your checking account and use it however you want. Or, if you have a separate business checking account, you can transfer money to your personal account. When you do either of these activities, it's called a "personal draw" in accounting lingo.

But, when you take money out of your business for your personal use, it's not a business deduction.

Some providers are confused into thinking that they won't be eligible to receive Social Security benefits unless they pay themselves a salary. No. You pay Social Security taxes on your profit, as shown on IRS Form 1040SE, which you should be filing with your tax return each year.

* This assumes that you are operating as a sole proprietor (self-employed). If you are incorporated as an S or C corporation, then the corporation would hire you as its employee.

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The answer is clear: No!

Family child care providers who have asked me a version of this question over the years are focusing on the taxes they pay, rather than the profit they earn.

Would you be better or worse off in these situations?

- You raised your rates, or started enforcing your late pick-up fees, or started charging a registration fee and earned $100 more per month
- The Food Program increased its reimbursement rates
- You won $1,000 in your state lottery

In all of these situations your taxes would be higher. But you would be better off after paying the taxes!

Let's look at the first example.

You earn $100 more per month, or $1,200 more for the year. You will pay 15.3% Social Security taxes on this amount, plus federal and possible state income taxes. Your income taxes will be based on your family's adjusted gross income and might range from a total of 15% to 30%. So, your total tax on the $1,200 will be somewhere between $360 (15.3% + 15% x $1,200 = $360) and $540 (15.3% + 30% x $1,200 = $540).

Therefore, after you pay these taxes, you will have somewhere between $840 ($1,200 – $360 = $840) and $660 ($1,200 – $540 = $660).

Are you better off with an extra $660-$840 in your pocket after taxes? Yes! Is this still true even though your taxes went up by $360 to $540? Yes, again!

So, do not focus on how much tax you are paying. Instead, look at your profit. You always want a higher profit, regardless of how much extra in taxes you will pay on this profit. Your tax rate will never be above about 45%, so you will always be keeping at least 55% of extra income/profit after taxes.

Buy more?

Sometimes providers ask me a slightly different question:

"My expenses are less this year than last year, so I'm think about buying more toys, so I don't pay more taxes this year. Should I do this?"

Whether you are trying to reduce your income or increase your expenses, my response is the same. Don't do it!

You never want to spend money just to get a deduction. If you spent $1,200 more in a year and were able to deduct it all, your taxes would go down by about $360 to $540. Your taxes would never go down by $1,200. Why spend $1,200 to get back $540 from the IRS? Instead, keep your money. Only spend it on things that are necessary to improve the quality of your program.

In conclusion: you always want more income, and you never want to spend money just to get a tax deduction.

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Should You Set Up a Limited Liability Company (LLC)?

When family child care providers think of incorporating their business, they often choose to set up a Limited Liability Company (LLC). This is a relatively new kind of business entity that could offer the limited personal liability of a corporation without some of the complex record keeping requirements.

To set up an LLC, contact your state's secretary of state office. There will be a filing fee of $40 – $500+ as well as an annual business fee. In most states, you will have to choose a business name and open up a separate business bank account.

As an LLC, you must keep your business and personal records completely separate. This can be a challenge since you cannot write personal checks out of your business account. You will have to pay for household expenses (supplies, food, repairs, etc.) out of your personal account and reimburse the business portion out of your business account. But you won't know the business portion (your Time-Space Percentage) until the end of the year.

The federal tax rules are exactly the same for a sole proprietor and a one-person LLC. This means you will file the same tax forms (Schedule C, Form 8829, and Form 4562), claim the same deductions and pay the same taxes.

The key benefit of an LLC is limited personal liability. The idea is that if a parent sued you, she could not get any of your personal assets (house, personal property, savings, etc.). There are, however, several problems with this.

First, since you are using part of your home for your business, the business portion is not protected by the LLC. This means that if your Time-Space percentage was 40%, then 40% of your home (and your furniture and other equipment) is business and would not be protected.

Second, since the LLC is a relatively new type of business entity, it's not clear if child care providers would really get the liability protection that is normally granted a corporation. I've heard from lawyers on this point and the law is unclear whether an LLC will protect you in a lawsuit over a major injury to a child.

I don't recommend setting up an LLC unless you understand the additional fees and record keeping requirements as well as the possibility that it will not offer you complete personal liability protection. In general, your best protection is to purchase a lot of business liability insurance ($1 million per occurrence and $3 million aggregate).

Don't listen to an attorney who tells you that all family child care providers should set up an LLC. It's more complicated than it may seem at first.

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Should You Share Your Rates Over the Phone?

A mother calls a family child care provider looking for care for their child. She asks the provider for her rates.

What would you say? Would you share your rates?

There is no right or wrong answer to this question. The majority of providers, in my experience, do not share their rates over the phone. Why?

They don't want parents to make a decision based solely on price. The provider wants parents to come and visit their home to learn about the benefits they offer when caring for their child. A parent who hears the price over the phone, and feels it is too high, may be reluctant to visit the home. They might be willing to pay the price once they saw the high quality of care.

A provider once told me the following story: A parent who had been with her program for a few days came to her and said, "When I called you to find out about your program and asked about your rates, you refused to give them to me. You told me I had to see in person what your program offered before we could discuss rates. At the time I called, I was only willing to pay a certain amount. After visiting your program and seeing the high quality of your care, I was willing to pay your higher rate. I'm so glad you didn't share your rates on the phone!"

The Other Side

Some family child care providers do share their rates over the phone with prospective parents. They do so because they don't want to spend time at an interview if the parent can't afford to pay their rate. There is no reason to spend an hour or more at an interview if your rate is $195 a week and the parent doesn't want to pay more than $140.

How to Handle the Call

Here's some examples of what I've heard from providers about how they respond to parents who ask about their rates over the phone:

- "My policy is not to share my rates over the phone. Please come and visit my home to see what I can offer your child. Then we can discuss my rates. My rates match the quality of care I offer."
- "I'm not the low-cost alternative."
- "I'm not the cheapest care in town. If you want the cheapest care, keep looking."
- "I charge above average rates for above average quality."

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Summer is the time for vacations, family outings, gardening, reading, and just plain rest.

For many family child care providers, summer is a time to reduce their hours of operation.

Taking some time off in the summer may be based on personal choice, or it may be a necessity because of a reduced demand for services. Some child care parents may withdraw their children for summer camps or family vacations. Other parents, such as teachers, work fewer hours in the summer and plan to spend more time with their children.

What are the tax consequences of reducing your summer hours?

When you work fewer hours, your income will go down. In addition, serving fewer meals and snacks means you will receive less reimbursement from the Food Program. One of the financial challenges of being a family child care provider is managing the ups and downs of your income as parents come and go.

Plan ahead when you know that your income will be less in the summer. Try to keep your expenses down during this time. Put aside some of the money you are earning the rest of the year to help you get through the slower summer months.

One of the biggest tax benefits of being a family child care provider is the ability to deduct a portion of your house expenses, including property tax, mortgage interest, rent, utilities, house insurance, house repairs, and house depreciation.

Time- Space Percentage

The amount of the deduction you can claim for these items is based on your Time-Space Percentage. This percentage is determined by how many hours you work in your home and how much space you are using in your home on a regular basis for your business.

If you are closed for a month or two during the summer, this should not make any difference in your space percentage. In other words, if you are using a bedroom for naps on a daily basis for ten months of the year and not at all for two months, you would still count this room as being used on a regular basis throughout the year.

If you are closed from a week to several months during the summer, this will have an effect on your time percentage. The fewer hours you work, the lower your time percentage, and ultimately the lower your home business deductions will be.

To help reduce this impact, keep careful track of all the hours you work during the summer. Include in this accounting all the hours children are at your home. This may be more complicated to track if you have children attending part days, or on an irregular basis.

Also, be sure to record all hours you are spending on business activities when the children are not present, including hours spent on activity preparation, cleaning, meal preparation, and special projects such as painting the playroom, building outdoor equipment, and reorganizing your records.

Regardless of the impact of reduced income and lower home deductions, it is a good idea to take time off each year for yourself. Family child care providers work very hard, and you deserve some days of rest. Enjoy!

Tom Copeland – www.tomcopelandblog.com

Ten Questions to Ask Before You Purchase Family Child Care Business Liability Insurance

All family child care providers should purchase professional business liability insurance to protect themselves against the risk of caring for children in their own home.

These risks are real: the children in your care can get injured, parents can sue you for child neglect or failure to adequately supervise their child, and so on.

Professional business liability insurance can reduce these risks so that you can sleep at night and not worry about any of this.

We strongly recommend that you shop around and get the details of an insurance policy from at least three insurance companies. Ask for a copy of the policy and compare coverages and price.

Use this Checklist to help you compare insurance policies.

1. What is the lowest limit available for "per occurrence" coverage ___________________________ and

   "aggregate" coverage? ____________________________

   What is the highest limit available for "per occurrence" coverage ___________________________

   and "aggregate" coverage? ____________________________

   "Per occurrence" is coverage for each incident. "Aggregate" coverage is the total amount the policy will pay out in a year. Ideally, you want the highest coverage.

2. Does the policy cover Professional or General Liability for me, my employees and volunteers? Professional ___________ General ___________

   A General Liability policy will only cover you if the parent can prove you were negligent. You want a Professional Liability policy that will cover you even if you aren't negligent. It covers you against accusations of failing to render professional services.

3. Will attorney fees paid by the insurance company to defend you lower the amount of the coverage under the policy limits? Yes _____ No _____

   You don't want attorney's fees to lower the amount of your policy coverage.

4. Does the policy cover for allegations of child abuse/neglect, including corporal punishment, physical and mental abuse?
   Yes _____ No _____

You want this type of coverage.

If Yes, what is the limit of the coverage? __________________
Does the policy cover child abuse/neglect allegations against me or any other individual on the premises? Yes __ No __

Ask to see language in the policy that describes who is insured.

5. If a child care regulatory agency holds an administrative hearing that could negatively impact my ability to care for children, will the insurance company pay for an attorney to represent me?
   Yes _____ No _____

   This is a nice benefit.

   If Yes, how much will the policy pay for the attorney fees? ____________

6. Is the insurance policy written for me ("individual policy") or is it written under a "master policy"? Individual policy _____ Master policy _____

   An individual policy will more likely cover you for specific risks associated with your particular circumstance.

   If coverage is under a master policy, is the aggregate limit shared by all policy holders? Yes_____ No _____

   If so, there is a risk that the policy will run out of money before you can make a claim.

7. Does the policy include accidental medical insurance? Yes _____ No _____
   If Yes, what is the policy limit for each enrolled child injured? ______________________
   Is the accident coverage "Primary" _____ or "Excess" ______

   If you have "primary" coverage this means your insurance company will pay a claim right away, rather than waiting to see if the parent's insurance will pay. The trade off is that primary coverage may be more expensive than "excess" coverage.

   Does the policy include coverage for all enrolled children injured on and off your premises? Yes_____ No _____
   Can anyone other than the children in care be added to the accident medical policy?

   Yes _____ No _____

8. What is the deductible for each claim against the liability policy? ________________
   What is the deductible for each claim against the accident policy? ________________

   Ideally, you don't want to have to pay for any deductibles.

9. How are the following exposures treated in the policy

	Covered	Excluded	Conditional
a. Owned Animals	______	_____	_____
i. Which dog breeds are excluded?	______	_____	_____
ii. What are the limits of the coverage?	______	_____	_____
b. Libel/Slander	______	_____	_____
c. Play equipment	______	_____	_____
d. Extended hours	______	_____	_____
e. Dispensing medication	______	_____	_____
f. Food preparation	______	_____	_____
g. Swimming pools	______	_____	_____
h. Corporal punishment	______	_____	_____

The more your policy covers you in these situations, the better.

10. Are there other options available to me under your insurance program?

	Yes	No
a. Loss of business property	_____	_____
b. Loss of business income	_____	_____
c. Homeowners insurance	_____	_____
d. Automobile insurance	_____	_____
e. Workers' Compensation insurance	_____	_____

Sometimes it can be better to purchase multiple insurance policies through one insurance company.

This checklist was created by the National Association for Family Child Care, Tom Copeland, and several insurance agents.

Tom Copeland – www.tomcopelandblog.com

Family child care providers are self-employed taxpayers who must report their business income and expenses to the IRS. It is important to become familiar with all of the IRS requirements for filing your taxes. To help you prepare for this, here are ten record keeping and tax tips to help you as you start your new profession. By following these tips, you will be better able to organize your records, claim the maximum legal deductions, and reduce your taxes.

Receipts

Keep receipts for every business expense. Your goal should be to have receipts for every penny of your expenses. Because most of the costs to clean, maintain and repair your home can be partially deducted as a business expense (light bulbs, toilet paper, garbage bags, snow shovel, etc.), collect receipts whenever you go to the drugstore, hardware store, etc. Record on your calendar when you go on field trips or travel because of business. A canceled check may not be as acceptable to the IRS as a store receipt.

When can expenses be deducted?

You must report all income from caring for children even if you do not meet or have not completed local regulation requirements. You should begin deducting business expenses as soon as you begin caring for your first child, even if you do not meet local regulations. The only expenses you cannot deduct if you do not meet local regulations are expenses connected with your house (utilities, insurance, taxes, interest, depreciation and repairs).

Food Expenses

Because food costs will probably be your single biggest expense, you should begin keeping careful track of the number of meals you serve each day, including meals that are not reimbursed by the Food Program. Multiply these meal counts by the standard meal allowance rate to claim food expenses without having to keep any food receipts.

Monthly Review

Do not wait until the end of the year to collect your receipts and other records. Conduct a monthly review to make sure you have everything in order. Keep your records in one place. Use envelopes to store receipts by category of expense. Make sure receipts are labeled and can be read. If you forgot to get a receipt or if you could not get one (parking meter, garage sale, etc.), make one of your own to remind you of the expense.

Estimated Tax

You may have to pay some federal income tax before the end of the year. To find out if you must pay estimated tax, estimate your income and expenses through the end of the year. If you will owe $1,000 or more in taxes, you may have to pay in quarterly installments due April 15, June 15, September 15 and January 15. There are a number of exceptions to this rule. See IRS Publication 505 Tax Withholding and Estimated Tax.

Employees

If you hire someone as a substitute or helper in your business, you should treat this person as an employee, which means you must withhold Social Security and income taxes for the employee and pay federal and state unemployment taxes. You may also need to purchase workers compensation insurance. Many providers treat helpers as independent contractors and do not withhold taxes, but this practice is not advisable. Only someone who is in the business of providing substitute care or is doing a special service could be considered an independent contractor.

Household Inventory

Your house and items in your house that are used in your business are being worn out at a faster rate than if you were not doing family child care. As a result, you can deduct or depreciate a portion of the cost of these items that you owned before you went into business. Conduct a thorough room by room inventory and list every item (furniture, appliances, lawn mower, etc.) in your house. Consult the Inventory-Keeper for a room-by-room listing of items.

Year End Expenses

Be aware that if you purchase 40% or more of items that last longer than one year during the last three months of the year, you may not get all the deductions for all of your capital expenses for that year. To avoid this "mid-quarter convention" rule, plan your purchases before October or after December. If you begin your business during the last quarter of the year, this rule will apply to you.

Time-Space Percentage

The number that will probably make the greatest difference on your tax return is your Time-Space Percentage. You will use this percent to calculate how much of your expenses for business and personal use can be deducted as a business expense. The more hours you work and the more space you use in your home, the lower your taxes. Track all the hours children are present, from the moment the first child arrives until the last child leaves. Add to this all the hours you use your home for business when children are not present doing cleaning, cooking, preparing activities, record keeping, interviewing parents, etc. (Carefully) Track at least two months of these hours on a calendar.

House Improvements

You should begin depreciating a portion of your house as a business expense. The amount of your house you can depreciate is based on the purchase price of your home (minus the value of the land) plus all home improvements made before you went into business. Go back and record all of your house improvements (new roof, furnace, remodeling, etc.). Save receipts. Get replacement receipts from contractors, if necessary. As a last resort, photograph the improvements and write down your best recollection of the cost and date it was done. Keep records of any house improvements you make after you start your business. When you sell your home, these house improvements may reduce the amount of taxes you may have to pay.

To be successful as a family child care provider, you will need to establish a professional, businesslike relationship with the parents of the children in your care.

This means you will need to take yourself and your work seriously and treat the parents as business clients, even if they are also friends or relatives.

You will be most successful if you are able to distinguish and find a balance between the caring attention required for child care and the focus required for managing your business.

Some child care providers find it very difficult to talk about money, rules, or expectations with their clients.

One factor that can greatly complicate this is growing so close to the children in your care that you leave behind your responsibilities as a business owner.

Do your clients respect your business?

Some providers have complained to me that the parents don't treat them like a business. Usually the reason this happens is because the provider doesn't act as if she is running a business.

You can establish a healthy business relationship by clearly communicating your rules and expectations. Doing so will help reduce and resolve conflicts and bring you the respect you deserve.

Basic elements of a written contract

The most effective way to establish your business relationship with parents is to use a written contract.

You are responsible for setting your own rules. Some states require providers to include certain terms in their contracts. Other than these requirements, you are free to put whatever you want in your contract and to create as many policies as you wish.

At the very least, your contract should contain these four basic elements:

Names of the parties: your name, the parents' names, the names of the children

Terms of the contract: There are two terms in a contract that are enforceable in court –

Time: The hours and days you are open

Money: How much parents owe you for your services: when payment is due, late fees, registration fees, field trip fees, etc.

Termination procedure: How will the contract end

Signatures: Both parents (if around) and yours

Sample contracts

If you need help with writing a contract, there are a variety of sample contracts available to choose from.

My book Family Child Care Contracts & Policies has a simple one-page contract as well as a CD with many different contract and policy examples you can cut and paste into a Word document to create your own.

Redleaf Press publishes a two-page contract template with carbon copies.

The contract is your primary tool to set your hours and rates and spell out how it will end. Review it once a year to make sure it meets your needs.

Tom Copeland – www.tomcopelandblog.com

Every year thousands of women (almost all women!) make the decision to become a family child care provider.

It's an important decision to take on a job that is not easy. The hours are long and it can be difficult at times to handle the multiple tasks of caring for children and dealing with parents. Although our society often does not appreciate and recognize the valuable work that you do, being a family child care provider is also very rewarding! So, here's a welcome to all new providers!

Caring for children from other families in your home is a wonderful job with many benefits. You have the opportunity to stay home and care for your own children. And you can earn money to support your family. Your work will make a big difference in improving the lives of the young children in your care.

By being a family child care provider, you will have access to a variety of resources and services to support your business. These include:

Training workshops to help you learn more about caring for children

Grants and other incentives to improve the quality of your care

Support and mentoring from other providers through your local and national family child care association (www.nafcc.org).

Contact your local Child Care Resource and Referral agency (https://www.childcareaware.org/resources/ccrr-search/) for more information.

There are also some major tax advantages of being a family child care provider:

You will be eligible to participate on the Child and Adult Care Food Program (https://www.fns.usda.gov/contacts/contact-map). This federal program will pay you hundreds of dollars a year per child for serving nutritious food. This can be a major source of income for you.

You must report as income all the money you receive caring for children. But you can also deduct many business expenses such as food, toys, supplies, car expenses, and many household items. You can also deduct expenses associated with your home (rent, property tax, mortgage interest, utilities, house insurance and more). These expenses will significantly reduce your income and keep your taxes low.

The profit you earn caring for children will help make you eligible to receive Social Security benefits when you retire.

Before you can become a family child care provider you will need to meet your state child care regulations. These regulations include having a safe home environment, having the proper work permit, purchasing certain toys and equipment, and passing background checks. Contact your local child care licensor for more information.

There are many reasons why you should join the tens of thousands of other people like you who enjoy caring for children from other families in their own homes. It's rewarding to see children grow and learn. It's a chance to stay home with your own children. And it's an opportunity to make some money.

Whatever your reason – welcome!

Tom Copeland – www.tomcopelandblog.com

The Business Side of Giving Gifts at Christmas

Christmas is a time of gift giving and many family child care providers give gifts to the families of the children in their care. Gifts range from homemade items (winter scarves, photo albums showing pictures of the child from the past year) to books, pillow pets, and gift certificates.

What are the tax consequences of giving gifts to children and their parents?

IRS rules say that you can deduct gifts as a business expense up to $25 per person per year. This means that if you give $25 worth of gifts (birthday cards, Christmas presents, Mother's Day gifts, etc.) to a child's mother and another $25 to the child's father, you can deduct the full $50. If you give gifts worth $15 to the mother and $45 to the father, you can deduct $40 ($15 plus $25).

If the children make something for their parents (decorate cards, clay figures, etc.), these are activity expenses not subject to the $25 rule.

The same $25 per person limit applies to gifts you give to the children in your care. A gift is something that only the child uses. However, the IRS Child Care Provider Audit Guide says, "[IRS] Examiners should not confuse expenses related to activities done with the children with gifts."

Let's say you give a toy as a Christmas present to a child. If the toy is wrapped and the child takes it home to open it, then it's a "gift" subject to the $25 limit. That's because only the child uses it. If the child opens the present at your home and the other children play with it, then this could be said to be an activity expense not subject to the $25 limit.

The difference between a gift and an activity expense may be a fine line. Certainly, all the expenses associated with a Christmas party in your home for the children in your care are 100% deductible. Such expenses may include party decorations, food, games, balloons, party favors, Christmas cookies and treats, etc.

When reporting these expenses on your tax return, don't use the word "Gifts" unless you are referring to gifts to parents or to items used exclusively by the child. Call everything else "Activity Expenses."

Tom Copeland – www.tomcopelandblog.com

Those who get paid for caring for children in their home are running a business. It doesn't matter if it's called Kith and Kin, Exempt Care, Legally Unlicensed Care, or Family, Friends and Neighbor Care. It doesn't matter if the person is only caring for relatives, or for one child of a friend. It doesn't matter if the amount of money paid for child care is less than $100 a year.

If money is exchanged for the care of children in the home of the caregiver, then the caregiver must face a variety of business responsibilities. Kith and Kin caregivers are often unaware of their business responsibilities when they decide to care for children. This lack of understanding can create problems of federal and state taxes, exposure to the loss of homeowner's insurance, greater risks of liability lawsuits, and conflicts with parents over payment.

Taxes

Anyone who earns money caring for children in their home is responsible for reporting this income to the IRS and to their state. Caregivers can also deduct business expenses, which will reduce their taxes on this income. If a caregiver is in compliance with their state regulations, she can deduct the same expenses for her business as a licensed caregiver.

In other words, if state regulations say that a person is exempt from these regulations if she cares for children from one unrelated family, then this person can deduct the exact same business expenses as a fully state licensed provider. If a state has a system for certifying or registering Kith and Kin caregivers and a person complies with these rules, then the caregiver may deduct all business expenses, which includes food, toys, supplies, car mileage, furniture depreciation, and house--related expenses such as utilities, property tax, house rent, house insurance, mortgage interest, house repairs, and house depreciation.

Kith and Kin caregivers who take advantage of claiming all of these business deductions on their tax return may discover that they have more deductions than their income. In this situation, caregivers should not show business losses year after year because the IRS will not allow it. Showing a very small profit each year is acceptable. Some caregivers (grandmothers, for example) may earn little other money besides child care fees. As a result, they may owe little, if any, federal or state income taxes. However, caregivers who show a profit of above $400 will always owe Social Security taxes.

Some Kith and Kin caregivers may also be eligible for other federal and state programs that assist low-income families (Temporary Assistance for Needy Families, Food Stamps, General Assistance, Supplemental Security Income, and more). The income eligibility for these programs is based on a caregiver's "net income," not their "gross income." "Net income" is defined as business income minus business expenses. As a result of the many deductions Kith and Kin caregivers can claim, their "net income" is likely to be very low and it is unlikely that any benefits they receive from such programs will affect them.

Insurance

Caregivers who bring children into their home expose themselves to greater risks of injury to children, lawsuits, and property damage. Virtually any injury to a child will be the responsibility of the caregiver. Licensed providers can protect themselves by purchasing business liability insurance, but Kith and Kin caregivers generally cannot get such insurance if they do not meet the highest regulation standards of their state. Many assume that their relatives and/or friends will not sue them if their child is injured. This can lead to tragic consequences.

In addition, although some homeowner's policies will cover the home and the contents of the home if the provider cares for fewer than six children, some policies don't provide coverage if the homeowner cares for even one child. In one state, a provider's roof suffered hail damage and a contractor was fixing it when he noticed a sign in the window that said, "Day Care." The contractor told the insurance company that there was a day care business in the home and the company refused to fix the damage because the homeowner's insurance policy did not cover day care. Most Kith and Kin caregivers have no idea that they may lose their homeowners insurance coverage by caring for just one child. Therefore, all Kith and Kin caregivers should talk with their homeowners insurance agent to make sure they are covered while caring for children.

There is a similar problem with car insurance if a Kith and Kin caregiver is using their car on a regular basis to transport children or for other business purposes. Most car insurance policies do not cover providers who use their vehicles on a regular basis in their business or will charge high commercial insurance rates. Again, talk with your car insurance agent about how you use your car for your business.

Contracts

A Kith and Kin caregiver may believe there is no need to prepare a written agreement with the parent describing the basic responsibilities of parent payment and caregiver work hours. However, the lack of such an agreement can create problems. Failure by the state to pay for care on behalf of a low-income parent may leave the caregiver in the lurch unless they have a written contract that states that it is ultimately the parent's responsibility to pay for the care. A clear but simple contract can eliminate confusion and make it easier for the caregiver to enforce their agreement.

What Can Be Done

Business responsibilities are probably the last thing that Kith and Kin caregivers think about when they start caring for children. But these responsibilities won't go away and ignoring them can have significant financial consequences. Caregivers should take advantage of the tax deductions when filing their business tax forms (Schedule C and Form 8829). Caregivers should talk to their homeowner's and car insurance agents about the impact of caring for even one child on their policies, and they should use a contract with parents. Those public and private agencies that work with Kith and Kin caregivers should share this basic business information to help them understand their responsibilities and protect themselves.

Tom Copeland – http://tomcopelandblog.com

Will parents of the children in your care give you a Christmas gift this year?

If they do, are there any tax implications?

Here are some examples of how family child care providers handle the possibility that parents will give them a holiday gift:

1. Posted a wish list on their bulletin board giving examples of gifts they would like to receive: supplies, toys, gift cards, cleaning products, etc.
2. Asked parents to jointly pick out one big gift (jungle gym, nice easel, etc.) from a wish list that they can all contribute towards
3. Asked parents who don't have as much money for donations of their time to help their business
4. Asked parents to make donations to other organizations (Toys for Tots, food drives, etc.) instead of gifts

Some child care providers are uncomfortable posting a wish list because they don't want parents to feel obligated to give any type of gift. You should not do anything that makes you uncomfortable. Often child care providers establish a wish list when there is a history of parents giving them gifts and the provider wants to take the opportunity to get something practical to help her business and the children.

Tax Consequences

If a parent gives you cash or a gift certificate, such as a Christmas or holiday gift, it's not taxable income. If the parent gives you a Christmas or holiday present such as a book, flowers, or any other item, it's not taxable income. If you spend the cash or gift certificate on something for your business or use the present (book on child development), you can deduct it under the normal rules of deductions.

If a parent gives you a "bonus" of $50 for the good job you did that year, this is taxable income. If the parent gives you a gift or present as partial payment for the care of their child, this is taxable income.

In other words, if the intent of the parent is to give you a gift or present to celebrate a holiday or birthday, it's not income. If the intent is to reward you for your work, it is income.

Tom Copeland – www.tomcopelandblog.com

Most family child care providers who hire employees do so primarily because they can expand their program and care for more children.

But there are a number of costs and benefits that should be considered before taking this step.

First, let's look at the benefits.

Increased quality of care that an additional adult can bring

Another adult you can talk to

The ability to help someone who needs a job; and

Increased flexibility that allows you more control over your schedule.

There is also a downside when you hire an employee.

You must pay a number of federal and state payroll taxes and file a series of tax forms

You must purchase workers' compensation insurance

Because you are responsible for virtually anything your employee does, you must take the time to properly hire, supervise and possibly fire employees.

The Financial Side of Hiring an Employee

Will hiring an employee actually increase your profit?

The answer depends on how many more children you enroll after hiring an employee. To take a close look at this, providers should examine the additional costs of hiring an employee compared to the additional income from enrolling more children.

Let's look at an example: Lainie Provider decides to hire an employee at the federal minimum wage of $7.25 per hour (your state minimum wage may be higher). Here are her additional weekly costs:

Wages: $7.25 per hour x 40 hours per week (overtime is due for more than 40 hours of work in a week) = $290

Payroll taxes (7.65% Social Security/Medicare tax + .6% federal unemployment tax) = $24

State unemployment tax: varies

Workers' compensation insurance: varies

Other employee costs (training, supplies, food, benefits, etc.): varies

Total weekly employee costs: $314+

To offset this additional expense, Lainie would have to enroll two additional children at $157+ per week to break even. This doesn't include the possible additional costs of food, toys and supplies needed for two more children.

I've created an online tool (Hiring an Employee Worksheet) you can use to plug in your numbers and quickly see how much you will need to charge to break even.

As a general rule, you won't increase your profit until you care for more than two additional children after hiring a full-time employee.

You should also consider what can happen if you have a drop in enrollment.

Let's say under your state's licensing rules you can care for no more than ten children, but with an employee you can care for up to fourteen children. You decide to hire an employee and you enroll two additional children under your state licensing rules. If one child leaves your program, you can't reduce your employee's hours, so you are likely to start losing money. To avoid this you would have to ask another child to leave to bring you down to the proper ratio and then lay off your employee because you wouldn't need her anymore.

Therefore, from a strictly financial point of view, I would suggest that you not hire a full-time employee unless you are confident that you can enroll (and keep enrolled) at least three additional full-time children.

For some providers, the non-financial benefits may outweigh the financial risks. I know of providers who are very successful and have several employees. I know of other providers who didn't realize the actual costs of hiring employees and found out later that their employee earned more than they did.

Plan ahead before making this decision.

Tom Copeland – www.tomcopelandblog.com

How comfortable are you that you are saving enough for retirement?

When I ask this during my training workshops, most family child care providers answer that they are not at all comfortable.

You know that you probably aren't saving enough for retirement. There are many reasons why. You don't earn enough. You are spending too much today. You don't know how to save for retirement. And so on.

There's usually always a good excuse why people don't save more money. But the main reason is because people make saving money their lowest financial priority. And this is a choice.

In other words, people could choose to make saving money a much higher priority, but they don't. People could spend less if they wanted to on eating out, or going to the movies, or buying shoes, or buying any item that is not a necessity.

When you are saving money for your retirement, you should be taking advantage of the significant tax benefits offered through IRAs.

By investing your money in an IRA, you can claim a tax deduction on your contributions. You won't pay any taxes on the interest your contribution earns each year. Instead, when you take your money out after age 59 ½, you will pay tax on your contributions and the interest it earned.

This tax deduction, and the fact that you will owe no taxes on your investments during the many years you are saving, will have a significant impact on how large your retirement nest egg will be.

Let's say you invested $5,000 a year and your money earned 8% per year. If you invested this money through an IRA, you would have about $167,000 after 20 years. This would be 28% more money after taxes than if you invested your money outside an IRA. That's a big difference!

There is one IRA option that works differently than all the others. This is the Roth IRA. With a Roth IRA your contributions are not tax deductible. But when you take money out of a Roth IRA, you will not pay taxes on your contributions or the interest it earned over the years. In the long run, a Roth IRA is probably a better choice than other IRAs.

Other than a Roth IRA, you may also be able to contribute to a Traditional IRA, SIMPLE IRA, or SEP IRA.

The deadline for making a contribution to your IRA is April 15th. The earlier in the year you save money, the more you will have in retirement.

Don't let the tremendous tax savings available with IRAs pass you by. Start by saving a small amount of money each month, even if it's only $5 a day.

If you saved $5 a day for 5 days a week you would have $1,250 at the end of the year. If you invested this in an IRA that earned 8% each year, you would have $19,127 at the end of just ten years.

It's never too late to save money. If you saved $10 a day at age 52 and earned 8% a year in an IRA, you would have $294,000 by the time you reached age 70.

Choose to save. You can do it!

Tom Copeland – www.tomcopelandblog.com

The Perils of Operating at a Loss

Family child care is a for-profit business. Although some child care providers do earn a reasonable income, many others do not.

In 2007 I surveyed over 500 child care providers for my book Family Child Care Money Management and Retirement Guide. I found that 74% reported a business profit of less than $20,000, and only 5% made a profit of $40,000 or more.

It's not uncommon that some child care providers occasionally show a business loss. What happens in this situation?

There are some limitations of what deductions may be claimed if a child care provider tries to report a loss on her tax return. The house expenses that appear on IRS Form 8829 Expenses for Business Use of Your Home cannot create or increase a business loss. Instead, un-allowed expenses can be carried forward to the next year.

For example, let's say you show $25,000 of income and $20,000 of expenses on Schedule C (before taking into account Form 8829 expenses). Your tentative profit is $5,000. If your house expenses on Form 8829 total $8,000, you will only be able to deduct $5,000 of them (which will create a zero profit) and roll over the other $3,000 of expenses to the next year.

A loss can only occur when your Schedule C expenses (not counting Form 8829 expenses) exceed your business income. Situations where a loss is possible include low enrollment, a majority of spaces filled by subsidized children for whom you are paid a low rate by the state, and high expenses for items such as food, supplies, toys, repairs, equipment, and depreciation. The loss of even one family can have a significant impact on your income, and many child care providers have lost families because of the current recession.

If you are going to show a loss, you should be aware of how the IRS looks at it. IRS rules say that when you start your business you are presumed to be trying to make a profit. As long as you show a profit three out of the last five years, the IRS will maintain that presumption. If you don't, the IRS may see your business as a hobby and deny your deductions.

Therefore, if you show losses three out of five years, you will likely attract the attention of the IRS. In my experience, child care providers who show losses in consecutive years are audited frequently. When this happens, the IRS won't conclude that you have a hobby, but they will be much more likely to disallow many of your business deductions.

My advice is to show a profit at all times, unless you are experiencing unusual circumstances. Showing a loss in your first year or two of business is not something to worry about. It's also acceptable if you have a major expense one year (car, swing sets or other equipment) that creates a loss.

If it looks like you will show a small loss one year, you may want to consider not claiming some business expenses to show a small profit. If you do show a loss, pay extra attention next year and try to claim a profit by cutting back on expenses.

Whatever you do, don't go overboard in showing losses, like this child care provider did in California.

The child care provider reported gross income of $321 her first year in business and $7,348 in her second year. But she also claimed $42,600 in expenses her first year and $63,733 her second year! She did everything wrong by claiming a cross-county ski machine, payments to wineries, more than $20,000 for meals, and more. In the end, the Tax Court did allow losses for both years totaling $6,100.

This case shows, that although it's possible to show a loss, you don't want to go through the agony of an audit unless you have to.

Tom Copeland – www.tomcopelandblog.com

The following incidents occurred in family child care homes. The amount of money shown is how much the child care provider's business liability insurance policy paid out in claims.

A day care child pulled down a bottle warmer on top of another child: $525,000.

A three-and-a-half-month-old child died of SIDS: $435,000.

An older child dropped an infant on the floor: $300,000.

A bookshelf fell on a child: $273,000.

A provider was accused of negligence in the death of a child: $240,000.

A two-year old was poisoned with E. Coli: $130,000.

A parent alleged that the provider's son assaulted their daughter: $118,000.

A child fell and broke her leg: $90,000.

A child fell off monkey bars: $75,000.

Every family child care provider knows that caring for children in her home increases the risk of damage to property and injury to children. There is no way to eliminate these risks, but there are many things child care providers can do to reduce them.

The most effective way of reducing the risks of your business is to purchase professional business liability insurance. Unfortunately, only a small percentage of all licensed child care providers have taken this step.

What would have happened in the above cases if the child care provider did not have business liability insurance? It's possible that she would have been stuck with a huge legal judgment against her that she probably could not afford to pay.

Some believe that it's not worth purchasing business liability insurance because they don't have enough personal assets to worry about a lawsuit. This is shortsighted thinking. Depending on the state you live in, you can still be in deep financial trouble, even if you don't have much money to your name.

Here's what might happen. Let's say that in one of the above cases the parent sues you for $300,000 when her infant is injured after being dropped on the floor by an older child. Without business liability insurance, you would have to hire a lawyer to defend yourself (and pay the lawyer even if you win). If the judge awards the parent $300,000 and you have no money to pay it, this is not the end of the matter.

Your state law may allow the parent to put a lien on your home, meaning that when it's sold the proceeds will go to the parent. You may be required to sell your IRA investments and some of your personal property (motorbikes, second car, etc.). If you marry, your new spouse's assets might be taken. If you get an inheritance, it might be seized. Clearly, this can be a financial nightmare for the rest of your life.

The risk of a lawsuit doesn't end if the parent decides not to sue you. I once got a call from a child care provider who said, "Thirteen years ago a child was seriously injured in my program and had to go to the hospital. I cared for the child for several years after the child returned from the hospital and then moved away and went out of business. Now the child is eighteen and is suing me for the injury that occurred thirteen years ago."

In most states, children can sue up until they reach age twenty-one for injuries suffered when they were minors. This child care provider did not have business liability insurance to defend her against this lawsuit.

You cannot afford to be without business liability insurance to protect yourself from the many risks of running a business. In most cases, good business liability insurance costs only a dollar or two a day.

Tom Copeland – www.tomcopelandblog.com

The Start-Up Rule: How to Claim Expenses Before Your Business Began

One of the most commonly overlooked business deductions for family child care providers is claiming expenses for items you owned before you went into business.

On the day your business began, you had a house full of items: tables, chairs, beds, play equipment, washer, dryer, freezer, lawn mower, pots and pans, beds, rugs, toys, snow blower, and so on. Most of these items you bought before you thought about becoming a family child care provider. But you probably used them in your business once you started caring for children.

The Start-Up Rule

The IRS Start-Up Rule allows you to deduct, in your first year of business, up to $5,000 of items you owned before you went into business. The $5,000 rule applies to the business portion of your items (usually your Time-Space Percentage). It doesn't matter if you bought the item specifically for your business or had it before you thought about becoming a provider.

First, conduct an inventory of all the items in your home. Take pictures of everything. Estimate the fair market value of each item at the time you first started using it in your business. Compare it to its original price. Use the lower number. Don't worry if you don't have receipts for these items.

List your items with their individual cost/value under one of following three categories:

Individual items costing/valued at $200 or less (called "Materials and Supplies" by the IRS)

Total up the number of items in this category. For example: washer $150 + dryer $100 + freezer $75 = $325.

You can deduct up to $5,000 of these items in one year. If you have more than $5,000 of these items, you must amortize the amount above $5,000 over 180 months (15 years).

For example, let's say your inventory shows you have 150 items, each valued at less than $200, with a total value of $14,000. Let's say your Time-Space Percentage (http://tomcopelandblog.com/?s=time-space+percentage+quiz&x=9&y=2) is 40% ($14,000 x 40% = $5,600). You can deduct $5,000 this year and amortize the additional $600 over 180 months, for an additional deduction of $40 this year.

Individual items costing/valued from $201 to $2,500

Total up the number of items in this category.

If the total value of these items falls under $5,000, you can elect to use the De Minimis Safe Harbor Election (IRS Section 1.263(a)-1(f)) Rule. When you elect to use this rule, these items become categorized as "Materials and Supplies" and you can deduct them in one year, using the Start-Up Rule. You must include any items costing $200 or less in this calculation.

For example, if you have $3,000 worth of items individually valued at $200 or less and $1,500 of items individually valued at $201 to $2,500, you can deduct the total ($4,500) in one year under the Start-Up Rule. If the total is more than $5,000, you must amortize over 180 months the amount over $5,000.

However, you can also choose not to elect the De Minimis Safe Harbor Rule. If you do so, you can choose to apply the 100% bonus depreciation rule. This rule allows you to deduct the business portion of these items without a limit on how much you can deduct in the first year. This rule applies to items purchased or first put into business use September 28, 2017, or after.

For example, you started your business in 2022 and your inventory shows you have $4,000 of items valued individually at $200 or less. You have another $3,000 of items valued individually at $201 to $2,500, for a total of $7,000. If you applied the De Minimis Safe Harbor Rule, you could deduct $5,000 in the first year and amortize the additional $2,000 over 180 months. If you chose not to apply the Safe Harbor Rule, you could deduct both the $4,000 (under the Start-Up Rule) and the $3,000 (under the 100% bonus depreciation rule) in the first year.

Individual items costing/valued at more than $2,500

These items are not subject to the Start-Up Rule and the business portion can be deducted in one year using the 100% bonus depreciation rule. This rule will expire after 2022 unless Congress acts to extend it.

For example, let's say your inventory includes $4,000 of items individually valued at $200 or less, $2,000 of items individually valued between $201 and $2,500 and a fence valued at $8,000 and a swing set valued at $3,000. You can deduct up to $4,000 of items costing/valued at $200 or less under the Start-Up Rule. You can then not choose the De Minimis Safe Harbor Rule and deduct the remaining $2,000 worth items costing/valued between $201 and $2,500 or less in one year using the 100% bonus depreciation rule. You can also deduct in one year the fence and swing set under the 100% bonus depreciation rule.

Summary

Conduct an inventory of everything in your home that you owned before you went into business and then used in your business. List the items under one of the three categories described above.

If the total cost/value of these items is less than $5,000, use the Start-Up Rule and deduct them in one year.

If the total cost/value of these items is more than $5,000, apply the Start-Up Rule to items costing/valued at $200 or less. Don't choose the De Minimis Safe Harbor Rule for items costing/valued from $201 to $2,500. Instead, deduct them in one year using the 100% bonus depreciation rule. Use the same bonus depreciation rule for items costing/valued at more than $2,500.

Is this complicated? Yes! But claiming these items can significantly reduce your taxes. Give your inventory list to your tax preparer. Don't let anyone tell you that you can't apply these rules as a family child care provider.

What creates the most stress for a family child care provider? It's not taking care of young children – it's dealing with parents.

A parent won't pick up on time.

A parent won't pay on time.

A parent won't follow one of your policies.

Usually conflicts with parents can be easily resolved after some discussion. But sometimes that's not the case. When I speak with child care providers around the country, I hear from many who are frustrated and angry with parents over a variety of problems.

Here's a tool that you can use to resolve most conflicts with parents.

I call it the Three Choices of Life.

When faced with a conflict, you have three choices:

1. **I am happy** – Let the parent do whatever they want concerning the issue in dispute and be happy with it. Life is too short to worry about every problem you face.
2. **I am not happy** – Tell the parent what they must do to make you happy. If the parent refuses to follow your rules, end your agreement and let the parent go.
3. **I quit** – If you are unhappy and unable to confront the parent to resolve the conflict, go out of business. This work is too stressful for you, and you will be better off doing a different job.

There are no other choices.

Let's look at an example to see how this tool works in practice. Your drop off time is 7am. However, you let one parent drop off her child by 6:15am because she needs to get to work earlier. Unfortunately, she is regularly late. You tell the parent that it's inconvenient for you to be ready every day at 6:15 when she is not showing up on time. She tells you that she expects you to be ready when she arrives. You are frustrated and feel like ending your contract with her.

What can you do?

I am happy – Continue to allow the parent to drop off her child when she wants, and do not object when the parent is late. Let it go. Be happy that you are able to care for this child.

I am not happy – If you can't be happy, then you need to decide what you can do to make yourself happy. You could charge the parent an early drop off fee. Make the fee high enough so you will no longer be upset when she shows up early. If no amount of money will make you happy, consider changing her drop off time to 6:30am or 7:00am. Do not allow the parent in your home before your new drop off time. Lock your front door. If you adopt this rule, it's likely that the parent will not be able to continue bringing her child.

I quit – If you are unhappy and can't enforce your rule that will make you happy, then it's time to quit family child care and do something else. It doesn't make sense to work at a job that makes you unhappy and doesn't pay you a lot of money.

What should you do?

I'm very serious that all three choices are reasonable one's for you to consider. Many child care providers have had parents who broke their rules and did not let it bother them. A few child care providers may be at the end of their rope and want to move on to another job.

Most child care providers are stuck in the second choice – they are unhappy, but they don't know how to fix things. It's your business and you are responsible for setting your own rules. In the end, you need to make your business work for you. In my experience, child care providers usually bend over backwards to try to resolve conflicts with parents. I've seen very few who have unreasonable policies or treat parents with disrespect.

When child care providers do put their foot down and enforce their reasonable rules, almost all parents will comply. If the parents won't comply, then it's best for them to move on. You are not the best caregiver for every child in the world.

The next time you are stuck in an unresolved conflict, give my Three Choices of Life a try! Let me know how it works for you.

Tom Copeland – http://tomcopelandblog.com

The Three Most Important Rules to Follow that Will Reduce Your Taxes

Keeping records is not a fun activity for most family child care providers.

But some record keeping activities are worth paying more attention to than others.

Here are the three most important record keeping rules you should follow that will save you the most money on your taxes.

One: Save receipts for all expenses associated with your home

You are entitled to deduct at least a portion of all expenses associated with maintaining, cleaning or repairing your home. This includes, toilet paper, light bulbs, welcome mat, dishwasher detergent, furnace repair, lawn mower, and so on. My book Family Child Care Record Keeping Guide lists over 1,000 allowable business deductions that can amount to thousands of dollars. If you're not sure if the item you bought is deductible in your business, save it anyway. You can sort out that out at the end of the year. The message here is: save receipts for everything!

Two: Keep a record of all the meals and snacks served to the children in your care

Most providers use the standard meal allowance rate in claiming their business food expenses. This rate is set each year by the IRS. Look for the current year rate here. You do not need to save any food receipts! Instead, keep a daily record of all the meals and snacks you serve. If you are on the Food Program, save your monthly claim form. But it's critical to keep a record for those meals and snacks that you serve for which you are not reimbursed by the Food Program. Forgetting to record one afternoon snack a day for one child for a year will cost you over $200 in a food deduction!

Three: Track all the hours you use your home for business use

Most providers do a fairly good job of tracking the hours children are present in their home. Your records should show the moment the first child arrived, and the last child left each day. If a parent picks up a child later or arrives on time but stays longer to talk to you, keep a record of the actual time the parent and child left.

Next, keep at least two months of careful records showing how much time you spent in your home on business activities after the children left: cleaning, parent interviews, activity preparation, meal preparation, time on the Internet (reading this blog!), parent phone calls, and so on. Use the average of these two months for the rest of the year.

Tom Copeland – http://tomcopelandblog.com

The Time-Space Percentage (T/S%) is the single most important number for a family child care provider to accurately calculate on her tax return. It will make the biggest difference in reducing your taxes.

The T/S% represents the proportion of your home that is used for business purposes. You will also use it to determine how much of your shared business and personal expenses can be deducted as a business expense. Such expenses include:

- House expenses: House depreciation, house improvements, house insurance, house repairs/maintenance, mortgage interest, property tax, utilities (gas, oil, electric, sewer, water, cable television, garbage) and rent.
- Shared business and personal expenses: cleaning supplies, land improvements (fence, patio, driveway, underground sprinkler system), personal property depreciation (furniture, appliances, play equipment, television, etc.), toys, yard supplies, and much more.

As you can see, these deductions can amount to thousands and thousands of dollars. That's why calculating your T/S% correctly is so important!

If you purchase an items that is used exclusively for your business, you can deduct 100% of the cost. But if it's also used by your family, then you can't deduct it all. Instead, apply your T/S% to determine your business deduction. Don't try to deduct 100% of a living room couch. If your own children only play with an item (say a toy) during day care hours, then you can still deduct 100% of the cost.

T/S% Formula

Your T/S% is determined by multiplying your Time percent by your Space percent.

Your Time percent is determined by dividing the number of hours you work in your home for business purposes by the total number of hours in the year. If you worked 11 hours a day (7am-6pm), that represents 2,860 hours a year. Divide this by the total number of hours in the year (8,760) and your Time percent would be 32.6%. You are also entitled to include all hours spent after children are gone doing business activities such as cleaning, activity or meal preparation, record keeping, parent interviews, and so on.

Your Space percent is determined by dividing the number of square feet in your home that you use on a regular basis by the total number of square feet in your home. Regular use means you use it for business purposes two or three times a week. If you used 2000 of the 2200 square feet in your home regularly for your business, your Space percent would be 90.9%.

If your Time percent is 32.6% and your Space percent is 90.9%, your T/S% is 29.63% (32.6% x 90.9%).

Enter your numbers for your T/S% on IRS Form 8829 Expenses for Business Use of Your Home.

Tom Copeland – www.tomcopelandblog.com

Every January I get many questions from family child care providers on the same topic:

"Do I have to give the parents in my program an end-of-year receipt?"

"Am I responsible for giving parents my Social Security number or EIN, even if they left owing me money?

"Do I have to complete IRS Form W-10 and give one to each parent in my program?"

The answer to all of these questions is "No."

There continues to be some confusion around this issue, so let's clear things up.

Most parents who pay a child care provider are entitled to claim a federal child care tax credit using IRS Form 2441 Child and Dependent Care Expenses. This form requires the parent to list the name, address, and identification number of the child care provider, and the amount paid to the provider.

The Instructions to Form 2441 tell parents they can use IRS Form W-10 Dependent Care Provider's Identification and Certification to collect the identification number of the caregiver. It's the parent's responsibility to give this form to the child care provider. It's not your responsibility to give Form W-10 to the parent.

Form W-10

Few, if any parents, however, are giving their family child care provider this form.

According to the law, family child care providers are not required to give parents their identification number and are not required to give parent receipts. If the parent left your program in 2022, you are not required to track them down to give them this information.

However, if you are on good terms with the parents in your program, I do recommend that you give parents an end-of-year receipt, along with your identification number.

If you do so, ask the parent to sign one copy and keep it in your records.

This can help protect you if you are audited and are asked to provide evidence of what the parent paid you for the year. Many providers give receipts to parents at the beginning of the year, but most don't keep a copy signed by the parent.

If a parent has left your program earlier in 2022, you can mail them two copies of the receipt (with a stamped envelope) and ask them to sign one and return it to you.

You can use the Form W-10 as your end-of-year receipt. Although the form doesn't provide a space indicating how much the parent paid, you can write the amount across the top of the form and have the parent sign a copy of the form that you keep in your records.

Form W-10 is included in the KidKare software program as well as in my annual Family Child Care Tax Workbook and Organizer. Redleaf Press also publishes a family child care receipt book.

You can also create your own receipt:

"Received by ______________________(your name) for child care services for the care of ________ (name of child) for 20__. Provider identification number __________ Signed _______________________ (parent) _________________________ (your name) Dated: __________"

If a parent left owing you money, I would recommend telling the parent that you will only give them your identification number once they have paid you in full. The only time you face a consequence is if the parent gives you a copy of Form W-10 and you fail to fill it out. If this happens, you face a possible $50 penalty. But since 99% of parents don't know they are supposed to do this, I wouldn't worry about it.

Don't give parents your Social Security number. Instead, get an Employer Identification Number (EIN) and use it to reduce the chances of identity theft.

Tom Copeland – http://tomcopelandblog.com

When family child care providers seek help from tax preparers, too often they receive bad advice because the tax preparer doesn't fully understand their business.

Here are four areas in the tax laws that are unique to the family child care business. Make sure that your tax professional understands them.

Following these rules will save you a lot on your taxes.

Household Deductions

All businesses can deduct expenses that are "ordinary and necessary" for their business. The definition of ordinary and necessary is helpful, typical, appropriate and useful for the business.

Since your business is providing a home learning environment for children, you are entitled to deduct hundreds of household items used in your business. This includes furniture, appliances, kitchen equipment, cleaning supplies, cable television, lawn care, service contracts on your appliances, new door bell, bedding, towels, floor polish, and so on.

Because of this, you should save every receipt for items that have anything to do with cleaning, repairing, or maintaining your home as a home.

My book Family Child Care Record Keeping Guide lists over 1,000 allowable business deductions.

Note: You can only deduct a portion of items used personally as well as for your business. Use your Time-Space Percentage.

If your tax preparer says you can't deduct a household item, respond by asking, "Where does it say in an IRS publication that I can't deduct this?" You may need to explain how a particular item is helpful, useful or appropriate for your business.

Business Use of Your Home

You are entitled to deduct a portion of the costs associated with your house: property tax, mortgage interest, utilities (gas, oil, electric, water, garbage), house insurance, house repairs, house depreciation, and house rent.

Claim the Time-Space % of these expenses on IRS Form 8829 Expenses for Business Use of Your Home.

Your Time-Space % is based on the number of hours you use your home for business and the number of square feet you use for business on a regular basis.

Time

The family child care business is the only one where you must add up all the hours you use your home for business activities.

You can count all the hours day care children are present in your home. Count from the moment the first child arrives until the last child leaves. Count the extra time if parents pick up their children late, children stay overnight, or children come to your home on weekends to play.

You can also count all the hours you use your home for business activities when children are not present. This includes hours spent on cleaning, lesson planning, parent interviews, record keeping, meal preparation, parent phone calls, time on the Internet, and so on.

Hours spent away from the home shopping or taking children to school cannot be counted.

Don't let a tax preparer tell you there is a limit on the number of hours you can count. I've won a Tax Court case where a provider worked 98% of the year caring for children. I've won another Tax Court case where a provider worked sixteen hours a week in her home when daycare children were not present.

Space

Unlike all other home-based businesses, you can claim a room as a business room if it is "regularly" used for your business. Regular use means using it for your business about two-three times per week. Children do not need to be in a room for you to count it as regular use (storage room, office, garage, laundry room, etc.). Such rooms can still be counted as regular use even if your state child care licensing rules prohibit children from entering them.

It's not unusual for many providers to use all of the rooms in their home on a regular basis for their business.

All other home-based businesses can only count rooms that are used "exclusively" for their business. However, family child care is the only business that can have both "regular" use rooms and "exclusive" use rooms. If your tax preparer challenges this, tell him or her to look at the Instructions to Form 8829, page 2 under the heading "Special Computation for Certain Daycare Facilities."

Food Program and Food Expenses

Family child care is the only home-based business that has the CACFP Food Program. All providers are better off financially if they join the Food Program.

Food reimbursements received from the Food Program are taxable income. Exception: reimbursements received for your own children are not taxable income.

You can deduct up to one breakfast, one lunch, one supper, and three snacks per day per child (if you serve them). Food served to your own children is never deductible.

Meals or snacks that are not reimbursed by the Food Program do not have to be nutritious.

You do not need to save any food receipts if you use the standard meal allowance method for claiming food expenses.

You must keep a daily record of all meals and snacks served to your day care children, particularly those not reimbursed by the Food Program.

Don't let your tax preparer tell you that your food expenses should not be more than your Food Program reimbursements.

Depreciation

You always want to depreciate your home because house depreciation represents a substantial business deduction for you each year.

You are entitled to depreciate your home if you are licensed, have applied for a license or are exempt from child care licensing rules. Therefore, even if you only care for one or two children and are not required to be licensed, you can still claim house depreciation.

When you sell your home, you will owe tax on the depreciation you claim or are entitled to claim. Don't let your tax preparer talk you out of claiming this depreciation.

You are entitled to depreciate all household items you owned before your business began that you later used in your business. This can include furniture, appliances, pots and pans, wall decorations, tables, chairs, beds, and so on.

Summary

Take advantage of all of these tax rules that benefit your business. My book Family Child Care Tax Companion is designed to help you and your tax preparer identify potential errors before you file your taxes.

Tom Copeland – http://tomcopelandblog.com

Tips for Successful Parent Interview

Interviewing a prospective parent is an important moment for a family child care provider. It can make the difference between a new client and a lost opportunity. Here are some tips to make your parent interview more successful:

1. Set aside enough time to go over the details of your business, including all the terms of your contract and policies. Point out the benefits of your program: how you will help the child learn and succeed. One of the best ways to do this is to show photos and letters of how well children are doing after leaving your program.
2. Describe your expectations of parents and ask about their parenting philosophy. Share how you would handle common discipline issues. Ask if the parent has experienced difficulties with other child care providers.
3. Offer a tour of your home. Emphasize the safety features of your home (covered outlets, gates across stairs, dangerous items locked away, etc.). Because health and safety are the top concerns of parents, you can't emphasize this enough.
4. Never rush into signing a contract. If you or the parent need more time before deciding – take it. Allow the parent to take the unsigned contract home to review.
5. Some providers do two interviews – one with the parent alone and another with the parent and her child to see how the child will fit in.

During an interview, you may want to look for these warning signs:

- Was the parent unreasonably late for the interview? It may be a sign of things to come.
- Is the parent uncomfortable talking about their values and expectations in raising children (especially if they are different from yours)? You want a parent who is willing to talk through future conflicts.
- Does the parent show a lack of interest in how you will be caring for their child? If so, you may later be frustrated in trying to involve the parent in addressing their child's needs.
- Does the parent show signs of inflexibility and unwillingness to compromise? If so, you may have trouble handling unforeseen problems.
- Are there signs that indicate problems in caring for the child that would be unreasonably difficult?
- Does the parent treat you with respect?

Tom Copeland – http://tomcopelandblog.com

If you are a family child care provider who is just getting started, you have a lot to handle: meeting licensing rules, designing a curriculum, promoting your program to parents, establishing a contract, and so on. Keeping good records is probably not high on your to-do list.

Many providers hate the idea of record keeping. They would much rather spend time with children. The bad news is that there are so many record keeping and tax rules that it can be overwhelming if you try to master them all at once.

The good news is that you don't have to master everything at once. Instead, focus on these three record keeping tasks. Performing these tasks will make the biggest impact on reducing your taxes.

One: Save receipts for all expenses associated with your home

You are entitled to deduct at least a portion of all expenses associated with maintaining, cleaning and repairing your home. This includes, toilet paper, light bulbs, welcome mat, dishwasher detergent, furnace repair, lawn mower, and so on. My book Family Child Care Record Keeping Guide (https://www.redleafpress.org/Family-Child-Care-Record-Keeping-Guide-9th-Edition-P1133.aspx) lists over 1,000 allowable business deductions that can amount to thousands of dollars. If you're not sure if the item you bought is deductible in your business, save it anyway. You can sort that out at the end of the year. The message here is: save receipts for everything!

Two: Keep a record of all the meals and snacks served to the children in your care

Most providers use the standard meal allowance rate in claiming their business food expenses. The rate for 2022 is $1.40 breakfast, $2.63 lunch/supper, and $.78 snack. The rates are higher in Alaska and Hawaii. You do not need to save any food receipts! Instead, keep a daily record of all the meals and snacks you serve. If you are on the Food Program, save your monthly claim form. But it's critical to keep a record for those meals and snacks that you serve for which you are not reimbursed by the Food Program. Forgetting to record one afternoon snack a day for one child for a year will cost you $203 in a food deduction!

Three: Track all the hours you use your home for business use

Most providers do a fairly good job of tracking the hours children are present in their home. Your records should show the moment the first child arrived, and the last child left each day. If a parent picks up a child later or arrives on time but stays longer to talk to you, keep a record of the actual time the parent and child left.

Next, keep at least two months of careful records showing how much time you spent in your home on business activities after the children left: cleaning, parent interviews, activity preparation, meal preparation, time on the Internet (reading this blog!), parent phone calls, and so on. Use the average of these two months for the rest of the year.

Summary

Do these three tasks and you are on your way to saving lots of money on your taxes. You may even find that record keeping can be fun!

Note to experienced providers: These three tasks remain the most important ones for you to follow each year regardless of how long you've been in business!

Tom Copeland – http://tomcopelandblog.com

Many family child care providers have received a grant from their state or federal government.

It may have been called a grant, stipend, emergency relief funds, CARES funding, or some other name.

It may have been a one-time payment or recurring payments.

It may have been in the form of supplies or equipment.

What are the tax consequences of receiving money or supplies/equipment from your state or federal government?

In all cases, grants are taxable income to you. Report this income on your Schedule C if you are self-employed. It's business, not personal, income. Your state may or may not require you to pay state taxes on this grant.

If you received supplies or equipment, report the cost of the items as income. If you don't know the cost, estimate their value.

You may or may not receive an IRS Form 1099 from your state reporting how much you received in grants for the year. You still must report grant money as income even if you don't receive this form.

The tax benefit of a grant

You are always better off financially if you do receive a grant. This is true even though it's taxable income. That's because you will never pay more than about 30-40% of the grant in federal and state taxes. In other words, you will always end up with more money after paying taxes on any grant. Therefore, never turn down a grant!

Examples

- If you got \$2,000 in grants and spent \$2,000 on supplies or toys or other items used exclusively for your business, you could deduct the full \$2,000. As a result, you would owe no taxes on the \$2,000.
- If you got \$2,000 in grants and spent \$2,000 on supplies or toys used by your business and your own children, you could not deduct the full \$2,000. Instead, you could deduct the business portion of the \$2,000, which would be your Time-Space Percentage. If this percentage was 30%, you could deduct \$600 as a business expense (\$2,000 x 30% = \$600). You would owe taxes on the difference of \$1,400. But, even if you were in a high tax bracket of 40%, you would owe \$560 in taxes. That would leave you with \$2,000 worth of supplies or toys that cost you \$560. Still a deal.

Note: Your state may say that their grant money is not subject to state income taxes. If so, it would still be subject to federal income taxes and Social Security/Medicare taxes when reported on Schedule C. Also, state grants are different than forgivable loans you may have received from the Small Business Administration (SBA). Any money you receive from the SBA Paycheck

Protection Program (PPP) or the Economic Injury Disaster Loan (EIDL) programs are not taxable income.

Your state may limit you on what you can purchase with your grant. Some states allow you to spend it on “wages” or “operating expenses.” That seems to me to mean you can spend in on yourself as payroll. If it’s not clear what you can spend it on, try to get clarification from the agency that gave you the money.

If you are not limited as to what you can spend this grant money on, what could you spend it on? You could make home improvements, contribute to your retirement fund, purchase additional equipment such as computers, children’s furniture, playground surfacing, a fence, and so on. If your state says you can’t spend the money on home improvements or retirement but does allow you to spend it on wages or operating expenses, you could use it for this and then use the money on home improvements, retirement and so on.

If you are receiving recurring stipends from your state, should you spend all of this money? Assuming you are free to allocate some or all of the money on wages or operating expenses, don’t feel you must spend the money once you receive it. It’s always better to save money rather than spend it. This is true even if you use the money to buy items for your business. Therefore, putting some money in an emergency fund, or paying off debt, or saving for retirement is always a good option rather than spending it.

Conclusion

All states have recently received millions of new dollars for child care assistance. Each state has wide leeway in how they can use the money. They can give out more grants, pay for equipment or training or other uses. Contact your local Child Care Resource and Referral agency to learn more about what your state will be doing with this money.

If there are new opportunities for you to receive a grant, take it! You will always be better off financially if you do.

Tom Copeland – http://tomcopelandblog.com

As a family child care provider, you can deduct the business portion of thousands of dollars worth of house-related expenses on your tax return.

These expenses include property tax, mortgage interest, rent, utilities, house insurance, house repairs, and house depreciation. You can also deduct the business portion of the cost of items you use for both business and personal purposes: toys, supplies, furniture, appliances, and much more.

The business portion of these expenses is based on a formula called the Time-Space Percentage. The Time Percent is based on the number of hours you use your home for your business and the Space Percent is based on the number of square feet you use your home on a regular basis for your business.

When calculating your Time Percent you can count all the hours children are present in your home (from the moment the first child arrives until the last child leaves) as well as other hours spent on business activities when the children are gone.

At the daycare.com family child care forum, providers recently compiled a list of business activities conducted after children were gone:

- Making out a grocery list
- Unloading groceries
- Cooking, preparing meals
- Cleaning up just before children arrive and after children leave
- Laundry (washing, drying, folding, putting away)
- Loading dishwasher (emptying dishwasher)
- Online research, webinars and visiting child care forums
- Cleaning toys, rotating toys, putting away and organizing toys
- Record keeping, entering data into KidKare software, working on taxes
- Baby/child proofing home
- Parent interviews
- Office work, filing, writing emails to parents, photo copying, writing newsletters, creating and updating your website/blog
- Cleaning finger prints off sliding glass doors/windows
- Writing contracts and policies
- Talking to parents on the phone
- Building a business website
- Communicating with parents via Facebook
- Placing ads on Craigslist and other online classified ad websites

- Food Program paperwork
- Conducting activities for local family child care association in home
- Reading magazines to find recipes
- Reading books by Tom Copeland
- Collecting items around the home for craft projects
- Planning and preparing children's activities (lesson plans, home decorations)
- Decorating playroom for themes and special days
- Putting together a daycare scrapbook or photo album

This is not a complete list. You can count hours spent on activities that you would not be doing except for the fact that you are running a business. So, you can count hours spent on putting together a photo album for parents and the children in your care because you would not do this if you weren't in business.

You cannot count hours spent on general housekeeping activities: cleaning out the garage, painting a deck, cleaning out gutters, washing the car, mowing the lawn, remodeling, making house repairs, cleaning a pool, defrosting the freezer, cleaning the oven, cleaning windows, etc..

We don't want to get too aggressive in counting hours on activities that would have done anyway.

When you clean areas that are used for both business and personal purposes, you can count the business portion of the time but not all the time. If it takes you 2 hours to clean the kitchen, bathrooms, and living room on Saturday, don't count all of this as business cleaning time. Instead, estimate the time that it took you to clean these areas because of your business – maybe 1 hour. Don't worry about being precise; the important point is not to count the entire 2 hours.

If you have a separate business freezer, you could count the time to clean it. If you have a separate play room you could count all the time to clean it.

It's not necessary to carefully track these hours every day of the year. Instead, track these hours for two months each year and use the average from these two months for the rest of the year. In fact, if you didn't keep good records so far this year, it's not too late to track these hours for the next month or so and use the average hours per week for the rest of the year. Then track two more months each year afterwards.

Enter all the hours you worked in your home on IRS Form 8829 Expenses for Business Use of Your Home, line 4.

Tracking the hours you work in your home after the children are gone is probably the single most important record keeping task you can perform that will reduce your taxes the most!

Tom Copeland – http://tomcopelandblog.com

Most family child care providers probably cringe at the thought of writing a business plan.

Creating a business plan is probably pretty low on your list of favorite activities. It isn't an exciting task, and may even seem quite intimidating, especially if you've never done anything like it before.

A business plan is a written tool that spells out how you will operate your family child care business and can include the following components:

- A start-up plan (for new businesses only)
- A statement of your hopes and goals for the business
- A marketing plan
- An insurance plan
- A program plan
- A professional development plan
- A record-keeping plan
- A financial plan (budget)

Paying closer attention to your business will have a significant payoff, and the hours you spend on planning may end up being the most important time you spend on your business, other than caring for the children.

Preparing a business plan is essential if you are starting a new business, but it is also very useful for an ongoing business, particularly if you want to apply for a business or personal loan. The business planning process offers several advantages:

- A chance to reevaluate and rethink your program. ("Should I try some new marketing approaches?")
- A financial spring-cleaning. ("Is it time to create a budget to help manage my spending?")
- A review of your practices to eliminate anything that's outdated. ("Should I overhaul my contract? Should I add more paid vacation time?")
- A review of your insurance policies to ensure you're adequately covered. ("Is it time to increase the coverage limits on my business liability policy?")
- Help in meeting your short-term financial goals. ("What changes would allow me to put more money into an emergency fund? Should I cut back on buying toys? Should I start charging for another federal holiday?")
- Help in meeting your long-term financial goals. ("What changes would let me save more money for retirement? Should I raise my rates? Add another child to my program?")

There are no rules about how to write a business plan or what to include. It can be as short as 4-5 pages or longer if you want. The goal is to set down some basics about your business that will help you focus on what is important. Here's a simple outline of a business plan:

Hopes and Goals

A short summary of what you want to accomplish in the coming year (having fun caring for children, meeting a budget goal, getting high marks from parent evaluations, etc.).

Marketing Plan

A list of 2-3 benefits of your program.
A schedule to contact your local Child Care Resource and Referral Agency (CCR&R) to update information about your program. Ask the CCR&R about rates charged by other caregivers (homes and centers) in your area.
An annual calendar of planned marketing activities.

Insurance Plan

An annual checkup with your insurance agent to make sure your home, contents of your home, and your car are fully covered for any business use.
An annual checkup to ensure that your business is protected through business liability insurance.

Program Plan

A written description of your goals for the number and ages of children you want to care for.
A description of your curriculum (formal or informal).

Professional Development Plan

Your goal for attending training workshops or classes for the upcoming year.
Your plan to achieve a post-secondary degree (if needed).
Membership in local, state, and national family child care associations.

Record-Keeping Plan

A written description of how you will keep records such as: children's attendance, parent payments, Food Program payments, business expenses, hours worked in your home, child care contracts, federal and state tax returns, and monthly bank statements.

Financial Plan

An annual budget and cash flow projection.

Getting Help

If you need help with developing your own business plan, don't hesitate to ask for assistance. You may want to talk to other providers who have already written such a plan. Or talk to your local CCR&R agency or Food Program sponsor for advice or referral to someone who can provide more help. Your tax preparer or financial planner may also be able to help you with certain areas of your business plan.

If it seems too daunting to write an entire business plan all at once, start by focusing on completing one section at a time. It may be easiest to start with a topic that you've already given some thought to or have some experience with.

For example, if you already have some ideas about your professional development goals, then start there. Once that section is done, move on to another area. There's no rush; try to make steady progress and you'll be done before you know it.

To be most helpful, your business plan should be a living document that evolves as your business changes and you gain experience. I suggest that you review and update your plan periodically — perhaps every year, or whenever there's a change in your personal business circumstances, such as an addition to your family or a move or expansion of your business.

Tom Copeland – www.tomcopelandblog.com

What is a Popsicle Worth to You?

With summer here, many family child care providers are serving more food to day care children outside of their normal meal patterns.

This may include serving fun food such as ice cream, popsicles, and other frozen treats. It may also involve eating out more at fast food restaurants and going on picnics or field trips.

Whether you are doing this a little or a lot, it’s important to keep track of all the meals or snacks you are serving.

This includes keeping track of all meals and snacks you serve that are not reimbursed by the Food Program. IRS rules allow all child care providers to deduct meals and snacks even if they don’t meet the nutrition standards of the Food Program. So, you can count a popsicle, ice cream, cookies, etc. as a snack.

I’m not telling you to serve junk food!

I am saying that if you do, you can deduct it. Using the Standard Meal Allowance rule, you can claim $.78 for each snack you serve (in Hawaii it’s $.91 and in Alaska it’s $1.27). These are 2022 rates.

You need to keep a daily record to claim all the summer meals and snacks you serve that aren’t reimbursed by the Food Program. You don’t need a food receipt, a menu or any record of what food you serve. Instead, all you need is a notation that shows which children ate how many meals and snacks each day.

For example, let’s say that Sally, Rebecca and Maria were served a treat (popsicle, ice cream, or pudding) each afternoon for a week. These snacks were not reimbursed by the Food Program. Here’s what you can record on a calendar or somewhere else:

- Monday pm snack – Sally, Rebecca, Maria
- Tuesday pm snack – Sally, Rebecca, Maria
- Wednesday pm snack – Sally, Rebecca, Maria
- Thursday pm snack – Sally, Rebecca, Maria
- Friday pm snack – Sally, Rebecca, Maria

If you use the KidKare software, you can track all un-reimbursed meals and snacks.

Recording un-reimbursed snacks is well worth your time. One snack for one child a day for a year (2022 rates) is worth a business deduction of $202.80. ($.78 x 5 days a week x 52 weeks).

What is a popsicle worth to you? Plenty!

Tom Copeland – www.tomcopelandblog.com

“Will it create a ‘red flag’ with the IRS?” is a common question I get asked at my family child care record keeping and tax workshops.

Many child care providers worry about putting something on their tax return that will create a “red flag” and attract the attention of the IRS.

“Will I get audited if I claim a Time-Space % above 40%?”

“Should I claim that I use all the rooms in my home on a regular basis?”

“Is hiring your own child a ‘red flag’?”

It’s human nature for family child care providers to worry about being audited by the IRS. We will do almost anything to avoid it.

The Short Answer

My general answer to these questions is, “If I knew what was a ‘red flag’, I wouldn’t tell you because then you wouldn’t claim what you are entitled to on your tax return.”

The Longer Answer

The IRS computers use complicated mathematical formulas to identify family child care tax returns for audits. What exactly will cause your tax return to be audited is a closely guarded IRS secret. In general, the more out-of-the-norm your tax return is from other child care providers, the more likely you are to be audited.

Here are two situations where you are more likely to be audited:

- You show large losses on your Schedule C for several years in a row.
- Your expenses for a particular line on Schedule C are way out of whack when compared with other child care providers. Let’s say you made $50,000 in income and claimed $25,000 in Supplies on line 22. This will probably attract the attention of the IRS because the supply expense is much higher than what most child care providers spend who make $50,000. No one knows what “average” child care providers spend on supplies by income, so it’s hard to know exactly what will trigger an audit.

The best thing you can do to reduce the chances of an audit is to not lump a lot of your business expenses onto one line on Schedule C. Many providers are tempted to put a lot of their expenses under Supplies because it’s often not clear what other lines to put their expenses on. If your largest expense on any one line on Schedule C is more than twice as much as the next largest expense, then you might want to spread out your some of your expenses over more lines.

On the back of Schedule C are several blank lines that you can use to list your Other Expenses (line 27a). Although there is no rule that requires you to put expenses on any particular line, I encourage providers to use the following expense categories for line 27a: Food, Toys, Cleaning

Supplies, Activity Supplies, and Household Items. These general categories can be used to cover many of your business expenses.

I list over 1,000 allowable business deductions in my book Family Child Care Record Keeping Guide and identify which line you can put them on your Schedule C. The Redleaf Press Calendar Keeper lists business expenses according to the order they appear on Schedule C and uses my Other Expenses suggested categories.

The KidKare online software program also uses my categories of business expenses.

The Best Answer

Don’t worry about being audited. Your chances of being audited are less than 2%.

Make sure that you have the records to back up the numbers you put on your tax return. Then, don’t worry if your numbers might attract the attention of the IRS. No one knows if they will. But, if your records are complete, you will be able to successfully defend yourself if necessary.

Claim the business deductions you are entitled to claim! The worst thing that can happen is that you get audited and might not be able to claim some of them because they weren’t “ordinary and necessary” business expenses. But, by not claiming some expenses to begin with, you are probably paying more taxes that you should!

Tom Copeland – www.tomcopelandblog.com

Not all Individual Retirement Accounts (IRAs) were created equal.

There are a number of different types of IRAs: Traditional, SEP, SIMPLE, and Roth. While there are some differences in their eligibility rules and contribution limits, all but one offer the same tax benefits.

That is, contributions to an IRA are tax deductible and interest earned on the contributions is not taxed until it's withdrawn.

The exception is the Roth IRA.

The tax benefit of a Roth IRA is substantially different than all other IRAs in that contributions to a Roth IRA are not tax deductible. In addition, contributions as well as the interest earned within the Roth IRA are not taxed upon withdrawal.

Basically, the Roth IRA gives you a tax benefit in retirement, while all other IRAs give you most of your tax benefit at the time of your contribution.

Let's look at an example. Sabrina Lopez is single, earns $40,000 a year and is in the 25% tax bracket. If she contributes $5,000 to any IRA except a Roth IRA, she will lower her taxable income by $5,000 and will save $1,250 in taxes ($5,000 x 25% = $1,250). However, if she contributes $5,000 to a Roth IRA, she will not save $1,250 in taxes because you can't deduct a Roth IRA contribution.

Let's say that she contributes $5,000 a year to an IRA for 20 years ($5,000 x 20 years = $100,000). Over that time, let's say she earns $65,000 of interest. If she contributed to any IRA except a Roth IRA, she would owe taxes on the $100,000 of contributions as well as the $65,000 when it is withdrawn, after she reaches age 59 ½.

If she contributed to a Roth IRA, she would not owe any taxes on the $100,000 of contributions and $45,000 of interest when it is withdrawn. In effect, she is giving up $1,250 in tax savings each year to avoid paying taxes on the $65,000 of interest in retirement.

Which IRA will give Sabrina the best tax benefit? As a general rule, the answer is the Roth IRA.

This is because with all IRAs, other than the Roth IRA, you must pay tax on the interest earned. There are scenarios where you could end up with more money if you invest with any IRA other than a Roth IRA, but these scenarios assume you will be in a lower tax bracket when you retire.

However, it's impossible to predict what the tax rates will be for you during your years in retirement. Therefore, I don't recommend basing your decision on which IRA to choose on future tax rates.

You can find a variety of calculators on the Internet that will compare the relative tax benefits of a Roth IRA and all other IRAs.

In addition to these tax benefits, there are other advantages to a Roth IRA over other IRAs:

You can withdraw your Roth IRA contributions tax-free at any time, even before you reach age 59½. Withdrawals of contributions from all other IRAs before age 59½ will result in a 10% penalty, as well as taxes owed.

You can withdraw the earnings on your Roth IRA contributions tax-free after you reach age 59½, as long as you have held them within the Roth IRA for at least five years, beginning with the first taxable year the contribution was made. If you withdraw earnings from your Roth IRA before reaching age 59½, you may owe taxes and penalties on your withdrawals. Withdrawals of earnings from all other IRAs are always taxable.

All other IRAs require that you start withdrawing your money after reaching age 70½. Not so for the Roth IRA. The Roth IRA allows you to continue to earn interest tax-free for as long as you want. If you decide to give your Roth IRA to family members in your will, they can avoid paying taxes on it as well.

Roth IRA Contribution Limits

The maximum you can contribute to a Roth IRA is the same as a Traditional IRA. These amounts can change over time. In 2022 the amount is $6,000 per year. If you are age 50 or older, you can contribute up to $7,000.

Closing

If you haven't thought about a Roth IRA before now, it's to your advantage to do so. Each year you wait before deciding to contribute to a Roth IRA, you will have less money in your retirement. With the tax and other benefits of a Roth IRA, it's well worth your while!

Tom Copeland – www.tomcopelandblog.com

What is the Measure of Your Success?

How do you know if your family child care program is a successful experience for the children in your care?

More importantly, how does a parent looking for child care know that their child will succeed if they enroll in your child care program?

The simple answer is that the measure of success of your program is how well the children succeed in life after they leave your program. Therefore, you need to show prospective families what happens to the children after they have left your program.

Here's how you can do this.

Keep track of the children after they leave your program. Write letters and send them birthday cards. Ask the children to write and send you pictures of themselves. You want to have pictures of them graduating from high school or college. You want pictures of their wedding, their new job, their growing family, and any other major life changes. Do this for as long as you are in business.

Post the pictures and letters on the wall or in your scrapbook or photo album. (Be sure to get their written permission before you do so!)

Here's how you use these pictures and letters.

When a prospective parent visits your program, this is what you want to say, "My most important goal is to help your child learn. I want your child to be successful once she leaves my program and starts attending school. I also want your child to be successful in life beyond their school years.

I believe that the best measure of whether or not my program will help your child be successful is for you to see how well children do after leaving my program.

I have enough experience working with children to know that my program works. To prove my point, look at this photo album. See all the children who have graduated from my program. This child is in college and doing well. This child now works at the downtown bank. This child is happily married and is now raising her own children. They are all doing well and getting ahead with their lives. I'm sure your child will also do as well if you enroll in my program."

How can the parent argue with this?

This strategy can be particularly effective with parents who are nervous about whether your program will match the values and expectations they have for their child. Maybe the parent believes in a lot of structure for their child, or instead wants a creative, child-directed curriculum. No matter. Because whether your program is highly or loosely structured, children who attend succeed later in life.

This strategy can also be effective with family child care providers with parents may be afraid to enroll their child with you.

Parents may be initially afraid because they don't know what goes on in the home once they drop off their child. They don't know if their child is going to learn and grow. Because a provider is alone at home with their child, they are nervous that the provider may not be the best caregiver for their unique child.

A display of photos and letters in a photo album or scrapbook that shows how children are doing after leaving your program, whether you are a home or center, can be a very powerful statement that what you are doing works.

(Now, if one of these children is in jail, get rid of their picture!)

Tom Copeland – www.tomcopelandblog.com

Do you feel buried in paperwork as a family child care provider?

There are enrollment forms, children's medical records, contracts and policies, permission slips, business receipts, tax forms, insurance policies, licensing forms, and so on.

All these documents are important, but some are more important than others. Also, how long do you have to keep them?

This is especially a problem for child care providers who have been in the business for many years. After 15 years in business you might need an entire room in your house to store all of these records!

So, what records should you keep, and what can you get rid of?

The general rule is that you don't have to keep any records, unless you are required to do so, or doing so will protect you. Therefore, you should save records to:

- Meet state child care requirements
- Protect yourself against a lawsuit
- Defend your tax deductions in an IRS audit

Meet State Child Care Requirements

As with everything else involving family child care, check with your regulator or licensor first. Your state may have rules requiring you to keep certain records for a number of years.

You may also want to ask your licensor what records they keep on you and for how long.

Protect Yourself Against a Lawsuit

Did you know that it's possible a child or parent could sue you years after they have left your program because of an injury suffered by the child while enrolled in your program?

It can happen. I once talked with a provider who had been out of business for ten years when she received a letter from a former child's lawyer announcing that they were suing her for an injury the child suffered in her program when she was three years old.

In general, children retain the right to sue until reaching the age of 18 and in many states they have additional years. For example, in Minnesota, everyone has the right to sue for six years after an injury. Children can sue up to age 18 plus one year. If a child is injured at the age of 12 years old, the child could sue until she reaches age 19.

Therefore, you need to keep the following records that can help you if you are sued: enrollment/termination records, injury reports/notes, and insurance policies.

You want to keep enrollment/termination records to show when a child was in your program. This can be important if it can be shown that the child was injured at a time she was not enrolled with you.

Whenever a child is injured in your program, keep an injury log that describes the accident and your actions. Even though you may have reported an injury to your regulator or licensor, it's in your own best interest to keep your notes on injuries and incidents. Many states will allow children to sue for sexual abuse even after the child reaches the age of majority.

To be sure that you can prove you had business liability insurance and to show the coverage amounts of your policy at the time, save a copy of your yearly business liability policies. If you have other insurance for your business, such as a rider for your car insurance or homeowner's endorsement policy, you will also need to keep these policies. Store these in a safe deposit box. Don't rely on the insurance company to have adequate records.

Keep all of the above records until the last child in your program reaches at least age 18 (or longer depending on your state law).

Defend Your Tax Deductions in an IRS Audit

IRS rules require you to keep your tax records for three years after you file them. If you have employees you should keep payroll records for four years. Your state may require you to keep your federal and state tax records for longer than three years.

Therefore, save all records associated with your tax return: receipts, cancelled checks, credit/debit card statements, record keeping calendars, photographs, and other written records. For items you are depreciating (home improvements), save these receipts for as long as you are depreciating the item, plus three years.

In my experience, when child care providers pay too much in taxes it's because they failed to keep these records.

Although you are not required to provide your daycare parents with a record of their payments, it's a good idea to do so.

Clean House!

Now that you know what records to keep and for how long, it's time to go through all your records and get rid of what you no longer need. If you buy a shredder to destroy your records, the shredder is tax deductible!

Tom Copeland – www.tomcopelandblog.com

An unhappy parent posts the following note about your family child care provider on the Internet, "Do not use the Sally's Home Child Care! She's incompetent and a scam. It was one of the biggest mistakes I have made."

You discover this information after Goggling your business name.

What can you do about this?

There are a number of Internet sites that contain parent reviews of child care providers: Yellow Pages; Yelp; About.com; and Insiderpages. So far, such sites have very few parent reviews of child care programs. (About.com has only 84 child care reviews nationwide, although this is likely to grow over time.) Facebook is another place where you may see negative comments from parents.

Unfortunately, we live in the age of the Internet where information can be widely shared and remain visible forever. It's painful to be the target of information that is false, hurtful and perhaps even illegal. This is a problem that is not going to go away.

The Internet, particularly social media sites, is a place where people are encouraged to share their opinions and ideas. Freedom of expression is good in general, but negative opinions and false statements can create real damage to your program.

What can you do?

Here are some steps to take when negative comments are posted about your program.

- **Talk to your licensor**: Whenever you hear or read that a past parent is saying negative things about you, contact your licensor. Explain what is happening and what the facts are. You want to protect yourself against a parent who later decides to make a complaint about your program.
- **Respond online**: When you see a negative review of your program online, ask other parents in your program to write a positive review on the same site: "Despite what someone has said, Sally's Home Child Care is very good. My kids love her!" Read the terms and conditions of these websites to see if the parent is violating them. If so, report it to the site. I have heard from child care providers who have been successful in having harmful parent comments removed.
- **Sue the parent?**: It's difficult to successfully sue someone for defamation (spreading of false statements that damage your reputation) because it can be hard to prove. It can also take time and money to hire a lawyer to represent you. Over the years I've talked with a number of child care providers who have had parents bad mouth their program to other parents in their community. Sometimes the complaints are serious, involving false accusations of child neglect (clearly slander).

  In every case, however, the parent stops making negative comments after a few weeks and the matter dies down. When negative comments are posted on the Internet, however, they remain there forever. Because of this, it's difficult to ignore. In general, I don't recommend filing a lawsuit unless the parent comments are so serious that they threaten the existence of your program.

- **Monitor your online reputation**: You want to know about negative comments about your program as soon as possible. Use Google Alert to track your name and your business name. You will get a weekly report every time they appear on the Internet. It's free. Periodically scan the rating sites identified earlier in this article to see if someone is posting about your program. Ask parents enrolled in your program to tell you if they read anything about you on the Internet. There are also services that provide assistance for a fee: Reputation.com; and Soicalmetrix.com (also in Spanish).

Tom Copeland – www.tomcopelandblog.com

What to do When a Parent Shows Up Drunk

One day a parent is picking up her child from your family child care home when you notice one of the following:

- The parent smells of alcohol
- The parent does not have a car seat for her toddler
- The parent is barely awake, or is acting erratically

You face two potential risks in these situations. If the child is injured in a car accident, you could lose your license. This is because child care providers are mandated reporters of child neglect, and the child in these situations is at risk. (If you are not certain that you would be required to report this, contact your state's office of child protection.)

In addition, the parent could sue you for failing to take steps to keep the child safe.

To protect yourself, you should adopt a transportation policy that will help keep children safe. Ask for the names of people who can pick up the child in an emergency. Call a cab. Tell the parent to go home and get their car seat and then return. Drive the child home yourself. Discuss other options with the parent. In the end, if the parent refuses to cooperate, call 911. Here's a sample transportation policy you can use.

When a parent shows up drunk or without a car seat, you need to take action and follow the steps in your transportation policy. If the parent demands her child, do not refuse to give up her up. Failure to give the child to the parent could expose you to a charge of kidnapping!

Do not act like one child care provider who told me she kept a baseball bat inside her front door to deal with disruptive parents. No!

Renew your transportation policy with parents upon enrollment so these situations do not arise. If they do, follow your policy. If the parent takes the child, don't hesitate to call 911 and report the license plate number.

Taking these steps will help keep children safe and protect your business.

Tom Copeland – www.tomcopelandblog.com

Parents picking up their children late is a common problem for family child care providers.

Your pick-up time is 6pm and a parent shows up late several times a month. Another parent always arrives before 6pm, but often doesn't leave your home until 6:20pm.

You work long hours caring for children - an average of eleven hours a day, according to several national surveys. It can be frustrating to deal with parents who want even more of your time.

What can you do to address this issue?

First, make sure your written contract states the specific times when parents are expected to drop off and pick up their children. The pick-up time can be different from one family to the next.

Second, state the consequences if a parent doesn't pick up her child on time. Most providers charge a late fee. Here are some examples:

- Parents who notify provider at least 2 hours before pick-up time that they will be late will not be charged a late fee.
- Parents who are late picking up their children once or twice in a month will not be charged a late fee. Parents will pay a late fee if they are late more often than this.
- Parents are given a fifteen-minute grace period and then are charged $.50/$1.00 per minute. (You could charge $.50 or $1 a minute for early drop offs.)
- Parents are charged $1-a-minute late fee if they pick up after the scheduled pick-up time.

In a workshop of mine a provider once said, "My contract states that if you are ever late picking up your child, you will be immediately terminated." That's strict! It worked for her, but I wouldn't recommend this rule to anyone else.

Time Versus Money

Before deciding on your late pick-up rule, consider this question: What is more important to you – your time or the parent's money?

If your time is more important, this means you don't want to work after your scheduled pickup time of 6pm. It doesn't matter how much money parents might pay you to be late, because you want to do other things with your time. Therefore, set a high late fee to ensure parents won't be late.

At one workshop a provider said she charged $50 a half hour late fee. However, her complaint was that one parent kept paying it! Since this fee wasn't deterring the parent from being late, I told her to raise her late fee for this parent. (You can have different late fees for different parents.)

If the parent's money is more important to you, this means you wouldn't mind working after 6pm if you were paid enough. If parents paid you $1-a-minute late fee, you could earn $30 for a half hour of work. This is a lot more than you are making per hour before 6pm.

However, most providers tell me that parents aren't consistently late if they have to pay $1-a-minute late fee. Therefore, you might want to set a lower late fee to make it more affordable! If you charged $.50 a minute, you would be earning $15 a half hour which is still a good wage. At the lower rate, more parents might not mind paying it, and you can earn some extra money.

One provider came up with a perfect solution in dealing with late fees. She said that late fees created tension and stress between her and her parents because they were associated with guilt and blame. Since she was willing to work a half hour after her pick-up time of 6pm, she announced to her parents that if they picked up between 6pm and 6:30pm, they would be charged an "evening rate" of $1 a minute.

No more late fees, because parents aren't late. No more stress because parents didn't have to rush to her home. It worked for the provider as well because she didn't mind working an extra half hour and being well paid for her time.

In the end, it's up to you to set your rules regarding late pick-ups and enforce them. You can ask the parent to pay the late fee at the time they are late, by the next morning, or add the fees onto their next regular payment.

Tom Copeland – www.tomcopelandblog.com

When a family child care provider hires a tax professional to do her taxes, she wants her taxes to be done correctly. She expects that her tax preparer understands the many unique rules affecting her business.

Sometimes, however, you may question how your tax preparer has filled out your tax forms.

What should you do if you disagree with what your tax preparer tells you?

First, say to your tax preparer, “Show me something in writing from the IRS that supports your position.”

If the tax preparer can show you that you are wrong, then accept it. But, if he or she can’t back up their position with a written authority, you should not let it go.

Ask the tax preparer to contact the IRS directly to seek a written authority. You could also contact the IRS yourself: 1-800-829-4933.

You can also contact me for help. Or you can ask your tax preparer to contact me (tomcopeland@live.com). I’m happy to point out what the IRS may have said about your question.

Here’s an example: Let’s say you want to deduct the business portion of car loan interest when you are using the standard mileage rate. Your tax preparer says you can’t deduct car loan interest unless you use the actual expenses method of claiming car expenses.

You say, “Show me something in writing that supports your position.” Your tax preparer won’t be able to. Then you say, “I’m not going to accept what you say without a written authority. Please research this issue and contact the IRS if necessary.”

In fact, IRS Publication 463 Travel, Entertainment, Gift and Car Expenses on page 15 says, “However, if you are self-employed and use your car in your business, you can deduct that part of the interest expenses that represents your business use of the car.”

Sometimes the answer won’t be so clear cut. Your tax preparer may say you can’t deduct your front door welcome mat because it’s not an “ordinary and necessary” business expense. This language can be found in IRS Code Section 162(a). Ordinary and necessary means typical, helpful, appropriate or useful for your business. Something doesn’t have to be indispensable for it to be ordinary and necessary.

There’s nothing in writing about welcome mats. You argue that parents and children use your welcome mat to wipe their feet and therefore it’s ordinary and necessary. Your tax preparer disagrees and says that it’s a personal expense. If you are at an impasse, you must make a decision whether to back down or insist that the welcome mat be deducted.

Sometimes you may disagree with your tax preparer because he or she is being too aggressive in claiming business expenses.

I heard this week from a child care provider whose tax preparer told her she could automatically claim that she worked 2 hours per day doing business activities when day care children were not present in her home. There is nothing in writing to support this position.

In fact, it's dangerous to claim any business hours unless you can back them up with some records to show the actual hours you worked. (The best way to show such business hours is to track them carefully for at least two months each year and use the average for these months for the rest of the year.)

If your disagreement with your tax preparer is over a few minor matters, it may not be worth pursuing. But if the disagreement is over a major issue, such as your Time-Space Percentage, then you may want to insist on seeing something in writing before you agree with your tax preparers' position.

If you can't agree on major issues, it may be time to consider changing tax preparers.

No one, including tax preparers, will always have the right answer. We all make mistakes. I make mistakes. However, you should not accept what a tax preparer tells you unless you are comfortable that he or she is giving you the correct information. Asking for something in writing from the IRS to back up a claim is a reasonable request.

Tom Copeland – www.tomcopelandblog.com

What to Give Parents: Social Security Number or EIN

Family child care providers should not give parents their Social Security number.

Parents want this number so they can claim the federal child care tax credit. They can use either your Social Security number or a business identification number.

The reason child care providers don't want to pass out their Social Security number is because of the growing problem of identity theft. Giving out your Social Security number to different families year after year increases the chances that it will fall into the wrong hands.

Instead, get an Employer Identification Number from the IRS and give this out to the parents of the children in your program. If you are hiring employees, you must get an EIN.

You can get your EIN at www.irs.gov. It will take you less than fifteen minutes to fill out the online screens after which you will instantly receive your number. Only one question may be confusing to answer: "Why is the Sole Proprietor requesting an EIN?" Unless you are hiring employees, answer "Started a New Business" even if you have been in business for years.

There is no fee to get your EIN. If you already have an EIN from a previous business, you can use the same number as a child care provider.

If you prefer, you can call the IRS at 800-829-4933 and get your EIN on the phone after answering a few questions.

Tom Copeland – www.tomcopelandblog.com

What’s Deductible in a Family Child Care Business?

Are you a new family child care provider who wonders what you can deduct as a business expense?

Or are you an experienced child care provider who wonders if you are claiming all the business deductions you are allowed?

Family child care is a unique business in which you can deduct hundreds and hundreds of items for your business. No other home-based business can deduct what you can deduct.

Let’s look at the general rule about claiming deductions.

You are entitled to deduct all expenses that are “ordinary” and “necessary” for your business. An ordinary expense is one that is “common and accepted” in a family child care business. A necessary expense is one that is “helpful and appropriate” in a family child care business. (See IRS Code Section 162a)

An expense doesn’t have to be indispensable for it to be considered “necessary.” In other words, you can deduct part of the cost of a dishwasher that is used to wash dishes used by the children, even if you could wash dishes by hand.

Here’s a partial list of expenses that could be considered “ordinary” and “necessary” for your business:

- Food – Using the standard meal allowance method, you can deduct $1.40 for breakfast, $2.63 for lunch or supper and $.78 for snacks. These amounts are for 2022. You can deduct this without food receipts.
- House expenses – property tax, mortgage interest, utilities, house depreciation, house repairs, and house insurance
- Furniture/appliances – washer, dryer, refrigerator, microwave, stove, dishwasher, rugs, sofa, tables, beds, chairs, TV, DVD player, lawn furniture, service contracts on furniture and appliances, etc.
- Household items – light bulbs, toilet paper, cleaning supplies, paper towels, laundry detergent, doorbell, welcome mat, clocks, etc.
- Home improvements/repairs – fence, patio, remodeling, new furnace, garage door opener, new floors, insulation, snow removal service, etc.
- Children’s supplies/equipment – arts and crafts, toys, playground equipment, floor mats, cribs, curriculum, etc.
- Other: food expenses for the children, car expenses (use the standard mileage rate ($.585 for 2022) or the actual expenses method), computers, wages to employees, advertising, etc.

My book, Family Child Care Record Keeping Guide lists over 1,000 allowable deductions!

Whether you can deduct a specific item depends on whether or not you use it in your business. If you use a sewing machine to make items for the children in your program, you can deduct part of its cost. If you don’t use your sewing machine in your business, you can’t deduct it.

It doesn't matter why or when you bought an item. If you bought a toy for your own child's birthday but she plays with the toy with the day care children, you can deduct part of the cost. If you started your business in 2018, you can depreciate all of the items you owned in your home before your business began, as long as you do use them in your business this year.

Consider this: You are running a business that provides a home environment for children to learn. Parents expect you to maintain your home as a home. Therefore, you can deduct the costs associated with maintaining/repairing/cleaning your living room, bathrooms, kitchen, play rooms, storage rooms, garage, and so on. This is what makes your business unique.

Unfortunately, this also means that some tax professionals don't recognize what "ordinary" and "necessary" means in your business. I've seen many situations where child care providers had to educate their tax professional (and sometimes the IRS!) as to what ordinary and necessary means to their business.

Note: This article discusses what you can deduct, but not how much of an item you can deduct. If you use an item 100% for your business, you can deduct all of it. If you use if for both business and personal purposes, you can deduct part of the cost.

In conclusion – Because of this broad definition of what you can deduct, make sure you save receipts for everything associated with your home! It's probably at least partly deductible.

Tom Copeland – www.tomcopelandblog.com

What's Not Deductible in Family Child Care?

"You can deduct it!"

This is probably the main message I've been spreading over the past thirty years to family child care providers across the country.

I've identified over 1,000 allowable business deductions in my book, [Family Child Care Record Keeping Guide (9th edition).]()

But not every expense is deductible in your business.

Obviously, items that are not used in your business cannot be deducted. If you use a sewing machine to make items for the children in your care, you can a deduct a portion of the cost of the sewing machine. But if another provider doesn't use her sewing machine in her business, she can't deduct hers.

Here are some expenses that are never deductible as a business expense:

- Club membership fees – Membership fees to health clubs, athletic clubs, airline clubs or hotel clubs are not deductible. Membership fees in professional organizations are: National Association for Family Child Care, local family child care associations, Chamber of Commerce, etc. Membership fees to Sam's Club, Costco, Amazon Prime are deductible.
- Personal portion of tax preparation fees – The cost to have your business tax forms prepared (Schedule C, Form 8829, Form 4562, Form 1040SE, Form 3115) are deductible. Personal tax forms (Form 1040, Schedule A, etc.) are not deductible (2018 rule). Have your tax preparer break out these costs.
- Estimated taxes – The estimated taxes you may be paying quarterly are not a business expense.
- First phone line into your home – It's not deductible even if you bought the phone to become licensed. You can deduct the business portion of a second phone line.
- Parking or speeding tickets – Not deductible, even if you are on a business trip!
- Charitable contributions – These are deductible as personal itemized deductions. If you give money to a local softball team so they will put your name in their program, you can deduct this as advertising.
- Personal clothing – Even though you may have special pants and shirts that you use only for your business, they are not deductible because they aren't a uniform. However, clothes that you wear for business that aren't suitable apparel outside your home are deductible. This would include smocks, story time aprons, or clown outfits. Sweatshirts or T-shirts that display a family child care logo or message are deductible as advertising. Clothing you buy for the children in your care are also deductible: mittens, caps, coats, etc.
- Pet care – Don't try to deduct expenses for your dog or cat unless it's for a leash or fence to keep them away from the children. Fish, gerbils, birds, turtles or other animals that you use to help educate children may be deductible. See more.
- Bad debt – If a parent leaves owing you money, you cannot deduct this as an expense. Instead, report only the income you actually received and pay taxes on this lower amount.

Do you love to create a budget? Probably not.

In a national survey of over 500 family child care providers, only 23% had prepared an annual budget for their business for the previous year.*

But, creating an annual budget is an important tool that can help you meet your financial goals.

A budget is a business plan of action, expressed in dollars. A budget estimates the income and expenses of your business for a specified period (usually one year).

What is a budget good for?

- *Planning ahead*
- *Promoting greater awareness of the overall operation of your business*
- *Creating an early warning system to help you control your expenses*
- *Guiding you in financial decision making*
- *Making it easier to set aside money to meet your financial goals*

I've heard lots of excuses from child care providers about why they don't have a budget:

- "It's too tedious and time consuming."
- "I don't make enough money to do a budget."
- "I want to spend money now and not worry about the future."
- "I'm afraid to find out how bad my financial situation is."

All of these reasons, in my opinion, are simply excuses for not wanting to face your financial future.

First Step

The first step in creating a budget is to identify some short and long-term financial goals. Short-term goals (1–5 year horizon) might be: buy a car, set up an emergency fund, pay off credit card debt, etc.

Long-term goals (10+ year horizon) might be: invest for retirement, create a college fund for your child, etc.

Once you set some financial goals, you will have more incentive to create a budget that will help you meet your goals.

A budget is a tool to estimate your income and expenses for the coming year. You could start by doing a budget for next year. First, estimate what your income will be from parents (by child), the Food Program, subsidized children, grants, and assorted fees. If you've never done a budget before, use the numbers from your last year's tax return (Schedule C).

Next, estimate what your expenses will be for next year. Again, you can use your last year’s tax return and experiences to help in your estimating. Create expense categories in your budget using the same expense categories shown on your last year’s tax return.

Subtract your total estimated expenses from your total estimated income. The result is your profit. (Let’s hope it’s a profit!) Now you can decide what you want to do with the profit. Obviously, you’ll take most of this profit to pay for your living expenses.

But, you can also plug in some amounts in your budget to address some of your short and long-term goals. Let’s say you estimated you will show a profit of $24,000 for next year. You could set aside some of this money towards your emergency fund, and some towards your retirement.

As the months pass you can adjust your budget to reflect actual income and expenses. A budget is not something that is set in stone! You can make changes.

Use your budget to help you become more aware of where your money goes, so you can decide if you want to maintain or change your spending patterns. Once you identify a financial goal and put it into your budget, you are much more likely to reach it!

At the end of next year, set up a budget for the following year. Your experience with budgeting this year will make the job much easier.

Although budgeting is not as much fun as caring for children, I urge you to give it a try!

I’ve created a sample budget on-line template that you can use to help you get started. I developed it as an added resource to my book Family Child Care Business Planning Guide, which discusses budgeting. Click on “Web Components” and then “Blank Budget Form.”

What are your budgeting experiences (pro and con)?

* See my book Family Child Care Money Management and Retirement Guide.

Tom Copeland – www.tomcopelandblog.com

What's Your Excuse for Not Purchasing Business Liability Insurance?

Business liability insurance protects family child care providers from the risks associated with caring for children.

These risks include:

- Injuries to children: A child breaks her leg falling off your backyard slide or a toddler loses his finger after catching it in your sliding-glass door.
- Lawsuits by parents: A parent breaks her arm after slipping on your icy front steps. Another parent accuses your son of inappropriately touching her child.

Despite these real risks, too many family child care providers don't have business liability insurance to protect themselves, their family and their business.

Here are the common excuses providers give for not having this insurance:

"I don't have any money, so why should I worry about a parent suing me?

Many providers incorrectly believe that they won't be sued because they have little money. If a child is seriously injured, the parent probably won't be deterred by your financial situation. If they do sue you, you'll have to pay a lawyer to defend yourself.

If the parents win a lot of money in court and you can't pay, they may be able to put a lien on your assets (such as your home), depending on your state laws. In some states, they can garnish up to 50% of your spouse's wages. If you quit child care and take another job, your wages may be garnished. You may also be required to sell some of your assets, such as a second car, a boat, and personal items such as a second television, golf clubs, guns, and so on.

Usually, a court judgment against you will last for ten years. If there is a lien on your home, it will be difficult or more expensive to borrow money in the future. Any inheritance you receive may be taken.

So, even if you think that you have nothing now, you don't want to be sued and possibly be responsible for paying a jury award for the rest of your life.

"I've never had an accident."

Not having had an accident before is no guarantee you won't have one tomorrow. Although you may never have had a car accident or had your house burn down, you're probably insured for these possibilities. The consequences of a lawsuit can have a much more serious financial impact than the destruction of your car or home.

"I can't be sued for more than my insurance coverage so why buy any more insurance than the bare minimum?"

Not true. You can be sued for any amount, and if you lose the case, you could be stuck with a lien on your home or other property and your wages garnished for many years to come.

"I have parents sign a contract that says I'm not liable if something happens to a child."

This won't help. Liability waivers can't prevent parents from suing you and judges won't enforce them. Also, the injured child could sue you later.

Summary

Look at business liability as the cost of doing business. The cost of business liability insurance is a few hundred dollars a year. It's 100% tax deductible. It will give you peace of mind.

Tom Copeland – www.tomcopelandblog.com

When Are Education Costs Tax Deductible?

You might think that classes related to your family child care business (child development, curriculum, record keeping, parent communication, etc.) would be deductible education expenses. Not necessarily.

Classes or workshops that you take before you were licensed are deductible, but classes or workshops that you are required to take to get a license are not deductible. So, in general, if you take a class on child development before you are licensed, it is deductible. However, if state law says that you have to have take a class in child development before you can get licensed, then it's not deductible. Classes that you are required to take after you are licensed to maintain your license are deductible.

Any training you receive after you meet your state's child care regulations is deductible as long as the training is related to your business (not classes on chemistry or engine repair!). Such training classes are deductible even if they don't qualify for training credit according to your local regulation requirements. In other words, if you take a class on record keeping that doesn't count towards your state training requirements, this class is still deductible.

All costs associated with obtaining NAFCC accreditation or a CDA are always deductible. Any classes to increase your skills to run your business are deductible. Classes offered by your local Child Care Resource and Referral agency are deductible.

College Education

You cannot deduct the cost of classes you take to receive a post-secondary undergraduate degree (any degree after high school) if this is your first post-secondary degree. The reason you cannot deduct this is because the degree qualifies you for a new occupation.

If you take college classes but are not trying to get a degree (classes on child development, for example), then they are deductible. If you already have a post-secondary degree and you are taking classes that qualify you for a second college degree (a degree in early childhood development or a master's degree in education, for example), then these classes are deductible.

(Yes, IRS rules can be complicated!)

I strongly recommend that family child care providers take every opportunity to improve their skills by enrolling in professional development classes and obtaining educational credentials such as the National Association for Family Child Care Accreditation, the Child Development Associate (CDA), and post-secondary degrees in early childhood education.

Time

If the cost of your class is deductible, then you can also count any time you spend on homework in your home when children are not present. If the class is not deductible, this time does not count.

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In which of the following situations could you deduct part of the cost of these meals?

1. You go out to eat alone on Friday night to relax after a hard week of work.
2. You and your husband go out to eat Saturday night and you talk about your business.
3. You take a parent out to eat on Saturday night after attending a move and talk about your favorite movies.
4. You go out to eat with members of your family child care association and discuss how to deal with parents who are late in picking up their children.

Answer: #2 and #4, maybe.

IRS Rules

Here are the IRS rules about when you can deduct meals eaten away from your home.

- You can never deduct a meal if you eat out alone, unless you are away from your home overnight for a business conference or activity.
- The meal must be directly related to the conduct of your business. Going out with a daycare parent or family child care association members for social purposes is not a business meal. If the purpose of your meal with association members is to listen to a speaker talk about your business, or if you have a substantial business discussion as a group, then you could deduct your meal.
- There must be a substantial business discussion at the meal. Going out to eat with your husband (who you have hired as your employee) and simply sharing how your day went would not meet this test.
- You must keep proper records for the meal. The records include:
- A receipt for the meal
- The name of the person you ate with
- The business topic you discussed
- The cost of the meal cannot be “lavish or extravagant.”

If you meet all of the above requirements, you can deduct 50% of the cost of the meal that you paid for (including the cost of your own meal).

Eating out with Family Members

The IRS will initially be suspicious if you try to deduct a lot of meals with your husband or your own children.

Don’t try to deduct weekly meals with your husband, even if he is your employee. I don’t think the IRS would accept this, as they would probably view it as a personal activity, no matter how much you talked about your business.

I have seen the IRS accept occasional meals with husbands, even when the husband was not an employee. How many meals are occasional? Maybe 5-10 a year. This is a guess. If you do spend a lot of time having a substantial business discussion at these meals because your husband is actively involved in your business, you could claim more meals.

This is a tricky area, because there are no firm IRS guidelines. You need to be "reasonable" when claiming business meals with family members. If you normally go out to eat once a week with your husband and he asks, "How was your day?" this does not create a business meal that you can deduct.

Employees

You can deduct the cost of any meal or snack your employee eats while working for you in your home. Although IRS rules say to save receipts and deduct the actual cost of this food, following this rule is extremely burdensome. Therefore, I would recommend using the standard meal allowance rate.

If you hired your husband or own children to work for your business, you could deduct meals you serve them if they work before and after the meal.

If you take an employee out to eat for dinner or a weekend meal, you must still have a substantial business discussion before you can deduct 50% of the cost. You must also keep the proper records as described above.

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When Should You Start Claiming Social Security Benefits?

One of the most consequential financial decisions a family child care provider can make is when to start claiming Social Security benefits.

You can begin receiving Social Security benefits as early as age 62, or as late as age 70. The longer you wait before collecting Social Security, the higher your monthly benefit will be.

Some family child care providers may want to collect Social Security benefits as soon as possible because of immediate financial needs, bad health, or other family considerations.

Waiting to collect also has its rewards: for every year you wait to collect after your full retirement age (age 66 or 67), your benefit will grow by about 8% a year. That's a lot.

The Social Security website has a Retirement Estimator (www.socialsecurity.gov) that can help you determine what your benefit will be depending on what age you start collecting benefits.

But, this estimator doesn't tell you when is the best time to claim your Social Security benefits and it doesn't take into consideration how to integrate your spouse's Social Security benefits with yours.

To get a more accurate estimate of your future benefits, use this free online calculator: www.opensocialsecurity.com.

It takes your age, marital status, and your estimated monthly Social Security benefit if you claim at your full retirement age, and tells you the best probability of when you (and your spouse) should start claiming benefits to generate the most money over your lifetimes.

The person who created this calculator also has written an excellent book Social Security Made Simple that I strongly recommend.

As I've said, this is not an easy decision and I strongly recommend using this calculator and then talking it over with a financial advisor before you act. You can find one by contacting:

The National Association of Personal Financial Advisors

Garrett Planning Network

These advisors charge by the hour and can help you make this important decision.

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For this article, I assume you are a family child care provider who has saved only a little for retirement, is a novice investor, and doesn't want to spend a lot of time learning about retirement investing.

If you have a little money to put away for your retirement, you want to put some of it in the stock market and some of it in fixed income investments such as money market funds, CDs, and real estate.

You want to invest some money in the stock market because that's where you have the best chance to earn a return that will exceed the inflation rate over time. As a beginning investor, you want to put your money in a stock mutual fund rather than investing in individual stocks.

In a stock mutual fund, your money will be used to invest in a variety of companies that meet the goals of the particular fund. For example, some funds invest in particular industries (health care, energy, transportation, etc.), or in the size of a company (small or large), or in the type of company (potential for rapid growth or payment of dividends).

But when you look closer, you discover that there are thousands of stock mutual funds to choose from. How do you decide which one to pick? Is it all guesswork? How can you make an intelligent decision?

When choosing where to invest your money for retirement, there is one factor that is critical to the long-term performance of the fund. Is it the past performance of the fund, the director of the fund, or the type of companies the fund invests in?

The answer is none of the above. **The most important factor that will determine the performance of the fund is the annual costs of the fund**, according to a 2004 study by Standard & Poor's, an investment research and rating firm. Since then, the basic conclusions of this study have not been challenged.

The study calculated the average expenses for nearly 17,000 mutual funds and then sorted the funds into two groups: those with expenses below the average and those with above-average expenses. The higher cost funds' average expense was 2.08% per year, versus 1.06% for the lower cost funds. So if you invest $10,000, you will pay about $100-200 per year in fees. Over time these fees add up.

How well do these funds perform? The study looked at the annualized returns of these funds over 10 years and found that the lower cost funds performed better than the higher cost funds in eight of nine fund categories. The annualized return of the higher cost funds averaged 9.17% while the lower cost funds averaged 10.94%–a difference of 1.77% each year!

This means that a higher cost fund must earn 1.77% more per year than the lower cost fund just to stay even in overall performance. Very few funds can achieve this over a long period of time. Therefore, you should pay close attention to the annual expenses charged by their fund.

You can find what your fund charges in expenses by looking at the prospectus published by each fund. If you didn't save a copy of your prospectus, you can look for it on the fund's Web site. Each prospectus must publish a chart that shows how much you would pay in expenses on a $10,000 investment after one, three, five and ten years. Use the ten-year comparison.

For example, the Oakmark Select Fund fees over ten years are $1,258 (Investor Class) whereas the similar fees for the Vanguard S&P 500 Fund are $179 (Investor Shares). Both fees are from 2021. This is a significant difference that will continue to grow over time.

Compare with Index Fund Expenses

When you look at the expenses of a fund you own or are considering investing in, make sure you are comparing expenses from similar funds. In other words, if your fund invests primarily in large companies, you should compare expenses with other funds that also invest in large companies.

The mutual funds that will consistently have the lowest expenses are index funds. *Index funds* follow a passive investment strategy by purchasing stock in companies that represent a benchmark and then holding onto the stock. (*Actively managed funds*, on the other hand, regularly buy and sell stock from different companies, thus increasing fees for the fund.)

The benchmark can be the S&P 500 (the 500 largest U.S, companies), the Russell 2000 (a representative of the smallest U.S. companies), or the Wilshire 5000 (a representative of all U.S. companies). There are many other types of index funds that track particular industries or other benchmarks. But the S&P 500, the Russell 2000, and the Wilshire 5000 are the most popular benchmarks that index funds track.

Here are some examples of index funds and their expenses as of May 2022 (using as a comparison a $10,000 investment over ten years):

Fidelity (www.fidelity.com)

Spartan 500 Index Fund (S&P 500 Index): $19

Small Cap Enhanced Index Fund (Russell 2000): $798

Total Market Index Fund (Wilshire 5000): $19

T. Rowe Price (www.troweprice.com)

Equity Index 500 Fund (S&P 500): $243

Small-Cap Stock Fund (Russell 2000): $930

Total Equity Market Index Fund (Wilshire 5000): $280

Vanguard (www.vanguard.com)

Large-Cap Index Fund (S&P 500): $64

Small-Cap Value Index Fund (Russell 2000): $90

Total Stock Market Index Fund (Wilshire 5000): $51

Use the above examples to compare against expenses in the stock mutual funds you are currently invested in. If you invest in index funds and pay attention to fund expenses, you will greatly increase your chances of getting a higher return for your money.

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Who Needs an Emergency Fund?

The obvious answer is that we all do.

Life is full of unexpected events. Are you ready for them?

- *Your car breaks down and requires a major repair.*
- *You fall and break your arm and are unable to provide child care for four to six weeks.*
- *Your roof springs a leak and your homeowners' insurance has a $1,000 deductible.*
- *Your mother becomes ill, and you leave town to stay with her until she recovers.*
- *The largest employer in your town shuts down, and three families tell you they are leaving.*

If you think about it, unexpected events are such a fact of life that we really should call them *expected* events.

Since you are almost guaranteed to encounter a major financial disruption at some time in the next few years, you should plan ahead by setting aside at least three months of living expenses in an emergency fund.

Deposit this money in a money market fund or bank account where it can be easily accessed and has little or no risk of losing its value.

Here's what three family child care providers said about emergency funds:

"*After five years of struggling, the best thing I did was to put six months' worth of living expenses into a savings account. This completely changed the way I did business, because I didn't have to worry about the money factor when making business decisions about terminating or enrolling new children."*

"*I think it's important for child care providers to have a plan B – a backup plan. Plan for bad weather, power outages, becoming ill and not being able to work, and car breakdowns and repairs. Think of everything you can that could affect your income, and develop a backup plan that will help offset the loss of income in those situations.*"

"*Make sure you have a three-month emergency fund before you spend any money on more supplies – and I actually feel you need more than three months. My goal is to have a six-to-eight-month backup fund. Because we have those reserves, if a family doesn't work out, I can feel okay letting them go.*"

Saving money for an emergency fund may not sound like an exciting project, but it's an important financial goal you should take seriously.

Don't let the prospect of setting aside three months of living expenses intimidate you. **The first step** is to set a specific goal ($5,000, $10,000, whatever three months of living expenses are for your family). Don't worry if this number seems impossibly high.

Second, establish a place where you are going to put the money and commit yourself to not spending this on anything except an emergency. It can be a separate savings account or a money market fund. Don’t put it into a Certificate of Deposit (CD), because there is usually a penalty for taking it out early.

Third, make regular (monthly) contributions to your emergency fund. Start small: $25 a month is fine. Maintain the discipline of a monthly contribution. To start with, establishing the habit of a consistent contribution is more important than the amount of the contribution. Review your progress at the end of each year and make plans for how much you will save each month next year.

Don’t be discouraged if your progress is slow. Slow but steady wins the race. As your emergency fund grows, so will your financial confidence. You will start to feel a sense of freedom and relief that will make all your hard work worthwhile!

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There are times when a tax preparer or the IRS will tell you that you can't deduct something on your business tax return.

When this happens, ask this question: "Why can't I deduct it?"

Sometimes you will hear this answer:

"You can't deduct _____ [names a household item] because you would be using it if you weren't in the family child care business."

This answer is wrong and let me explain why.

Ordinary and Necessary

The first response you want to give to someone who tells you that you can't deduct an item is "Can you refer me to something in writing that supports your position?"

More often than not, the person will not be able to.

The IRS tax code Section 162(a) says child care providers can deduct all "ordinary" and "necessary" expenses for their business.

Ordinary and necessary means: common, accepted, helpful, or appropriate. See IRS Publication 535 Business Expenses, page 2.

There is nothing in the IRS code or any IRS publication that says you can't deduct something unless you bought it specifically for your business, or you would use it even if you weren't in business.

IRS Child Care Provider Audit Technique Guide

The IRS Child Care Provider Audit Technique Guide gives a number of examples of items that family child care providers can deduct in their business: furniture, appliances, lawn mowing service, laundry facilities, computers, kitchen equipment, playground equipment, toys, etc.

The Audit Technique Guide also refers to items a provider might own before she goes into business and then describes how to deduct them.

Clearly, there is written support for the proposition that items you use for personal purposes can also be deducted as a business expense.

You can deduct an item if it's ordinary and necessary for your business, even if you would still use the item if you weren't in business. I've been defending providers in IRS audit for decades and I've never seen the IRS successfully argue this faulty position.

You can deduct an item based on how it's used in your business, not why it was purchased or the fact that it's also used personally and will continue to be used personally after you are out of business. After you have retired, you will continue to use your furniture and appliances and kitchen utensils and welcome mat and lawn mower and so on. They are still deductible while you use them in your business.

Story of the TV

Here's one of my favorite stories:

Years ago, I had a discussion with a tax preparer about which tax form to use to deduct a television. To settle the matter, I called the IRS and pretended to be a family child care provider.

"Where can I deduct my television?" I asked. The IRS official said, "You can't deduct your television." "Why can't I deduct it?" I replied.

"Because you used your television before you went into business." I responded, "But I also used my couch and washer and dryer. What's the difference?"

There was a long pause, then he said, "Well, I guess you can deduct it." I hung up.

It pays to ask the question "Why can't I deduct it?"

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Will You Owe Taxes When You Sell Your Home?

A family child care provider faces two potential taxes when she sells her home. One you can probably avoid and another you cannot.

Tax on the Profit

First the good news. You can avoid taxes on the profit on the sale of your home if the profit is less than $250,000 and you are single, or $500,000 if you are married. (Note: legally married same sex couples can now take advantage of this tax break.)

So, if you are single and bought your home for $150,000 and sell it for $400,100, you will owe taxes on $100 ($400,100 – $150,000 = $250,100) because the amount above the $250,000 exclusion is $100.

If you are married, you would owe no taxes on the profit because it's less than $500,000.

As you can see, most family child care providers will not owe any tax on the profit on the sale of their home.

Tax on the Depreciation

This second tax is not avoidable. You will owe taxes on the amount of depreciation you were entitled to claim on your home since May 1997.

This is true even if you didn't claim home depreciation on your tax return!

Let's look at an example. Rosalie Ryder purchased her home in 2008 for $200,000. Her Time-Space Percentage is 40% each year. She is entitled to claim a depreciation deduction each year of about $2,500 ($200,000 x 40% = $80,000 divided by 39 year deprecation rule = $2,500)

Rosalie does child care in her home until she sells it on December 31, 2021. She used her home for her business for 13 years. She will owe taxes on the amount of depreciation she was entitled to claim for the past 13 years, or $32,500 (13 x $2,500 = $32,500).

What if Rosalie didn't claim house depreciation for some or all of these years?

She would still owe taxes on $32,500! The IRS rule says that if you are entitled to depreciate your home, you will owe taxes on this depreciation even if you didn't claim it. Therefore, always depreciate your home!

Don't let someone tell you, "Don't depreciate your home because you will have to pay more taxes when you sell your home." Since you will have to pay these taxes anyway, there is no reason to give up the tax benefit of claiming depreciation. You will always come out ahead financially when you depreciate your home because the taxes on the depreciation will be less than the tax benefit of claiming the depreciation.

You will owe this tax even if you stop doing child care for years before selling your home.

The tax you will pay will be based on your tax bracket in the year you sell your home. For 2021, this could be either 10%, 12% or 22% or 24% on the house depreciation.

So, Rosalie will owe between $3,250 and $7,800 in taxes. Remember, she will owe these taxes even if she didn't depreciate her home.

Note: I've simplified the above example to exclude the value of land, home improvements, and expenses associated with the sale of the home.

Other Issues

If you show a loss for your business in one year, you won't be entitled to claim house depreciation for that year. Therefore, you won't owe tax on home depreciation for that year.

If you are single and live with someone else who owns the home, you aren't entitled to claim house depreciation and therefore won't owe any taxes on it when the home is sold. If you are married and your spouse (including legally married same sex couples) owns the home, you are still entitled to claim house depreciation and so would owe this tax.

If you haven't been claiming depreciation on your home, you can recapture all previously unclaimed depreciation by filing IRS Form 3115 Application for Change in Accounting Method. If Rosalie had not depreciated her home between 2007 and 2020, she can claim $32,500 of previously unclaimed depreciation using Form 3115 by filing it with her 2020 tax return.

Conclusion: if you are thinking about selling your home, talk with a tax professional who can advise you about the tax consequences of home depreciation.

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You Are Being Investigated, Now What?

by Frank S. Perri, Attorney, CPA

There probably has never been a day care that has not had to deal with a child getting hurt. Perhaps the injury was minor and easily cured by basic first aid. However, what if a child gets hurt so badly that medical attention is required? What would happen if you, a day care provider, are investigated by a state agency like a department of children and family services? Medical professionals are usually required by law to notify such agencies if there is a possibility that a child was abused or neglected.

This article explains what providers can expect if they are formally investigated by a state agency for possible abuse and neglect of a child. Because of the attention that child abuse cases receive, a provider may also be subject to criminal prosecution. This article also describes providers' rights under a criminal investigation, since it is not uncommon for a state agency investigation and a criminal investigation to occur simultaneously. I will not focus on whether or not a provider abuses a child, but rather on how he or she should conduct herself during an investigation. For the purposes of this article, I will assume that an accident has occurred and that the state agency is investigating the cause of the child's injury because it's obligated to do so.

How a provider handles a state agency investigation sometimes determines whether there will be a criminal investigation at all. In fact, her behavior during a criminal investigation may contain far more severe consequences than a state investigation. Thus, it is very important that providers take note of my advice. There are inherent risks in running a day care business. Understanding these risks and my suggestions for managing them will help you get through an investigation with the least amount of stress.

State Agency Investigation

If you have to take a child to a hospital to receive medical care, you should prepare yourself for a formal investigation by the state agency, probably the one that issued you your day care license. In this article, I will try to address the major questions that most providers would encounter, such as: Should I talk to anyone about the incident that led up to the injury? Do I have to speak to the state investigator concerning the incident? If I refuse to speak to the state investigator, what could happen? Should I talk to an attorney, and if so, what kind? Can I have an attorney with me if I decide to cooperate with the investigation?

Are providers required to participate in a state agency investigation?

Most state child care laws require child care providers to participate in investigations of their business. If you refuse, the agency has the right to revoke your day care license—and, given that the agency cannot risk exposing other children to possible abuse and neglect, they probably will.

What should the provider do to prepare for the investigation?

First of all, you should try to remember the events that led up to the child's injury. Try to remember who was present, what time it was, where it occurred and how the injury happened.

Remember that the more accurately you can answer basic questions, the more confident and less stressed you will be under investigation. Assuming that the injury was an accident, don't worry that you will be labeled as a child abuser; accidents occur all the time. Unfortunately, some providers do not handle the state investigation properly, which leads to criminal charges.

For example, let's say you speak to the state investigator and tell inconsistent stories of how the accident occurred, or you tell those who were present during the accident to lie to the investigator. You will not only have your license revoked, but will have opened the door to criminal prosecution. It is extremely important not to lie to a state investigator about the facts of the case.

Yet when I represent providers, I often have to explain that even though the child's injury was an accident, lying during an investigation carries criminal penalties, including jail time. Lying during an investigation is called obstruction of justice and is usually classified as a felony for which you can be sent to prison. The fact that you did not know that lying during an investigation was a crime is not a defense. Your attorney cannot use your ignorance of the law to help your criminal case if you are arrested for obstruction of justice.

Many providers would never face criminal prosecution if they had properly cooperated with the state investigation. Thousands of child care providers have to take children to the hospital because of accidental injuries. This is not an uncommon event, and providers do not need to fabricate facts to save face. State agencies are not blind to the fact that children get hurt. However, they are obligated to investigate injuries, and lying about what happened will not help your case.

Should you hire an attorney, and if so, what kind of an attorney?

This is a tough question, and I would say it depends on how competent you are in explaining facts accurately, especially during a stressful period. If you are not good at communicating, then I would recommend that you hire a criminal defense attorney because of the possibility of criminal charges. If you are contacted by a state investigator, tell the investigator that you will have your attorney with you during the interview. There is nothing to stop you from having an attorney present, as long as you are cooperating with the investigation.

Moreover, you should be aware that the state investigator does not represent you, nor is the investigator required to look after your interests. On the contrary, it is the investigator's job to determine whether you did something wrong to a child. If you lie to the investigator, he or she will notify the local law enforcement authorities, and they'll begin a criminal investigation. This is often how police officers become involved in day care investigations.

One of the benefits of having an attorney is that he or she can interview you professionally, as an investigator would, so that you can resolve gaps in your testimony. All too often, the way we think about something is not how we communicate it. An attorney will help you get your facts straight and relay them clearly.

Keep in mind that hiring an attorney does not mean you did anything wrong. Sometimes people incorrectly assume that consulting an attorney implies a guilty mind. An attorney will help you to think of facts that you may not have considered. As your delivery of the facts becomes easier, your confidence will improve and your nervousness will decrease. The attorney will probably say that they should be present during the investigation, and that advice should be followed. After all, your livelihood is at stake.

Should I talk to anyone about the incident?

It is important that you not talk about the incident with anyone. The state investigator will talk to people with whom you may have discussed the incident. If what you told a third party is different from what you told the investigator, the investigator may assume that you are lying. Again, even if you are not lying, you are creating a perception of not telling the truth. Under no circumstance should you disclose facts to other people, even though you may be tempted to talk about them. It is natural for a provider to feel badly about what happened to a child. If you feel you need to talk, then speak to your lawyer; such conversations are protected by attorney-client privilege, and the investigator cannot get your lawyer to disclose what you said.

Will I have to pay for an attorney?

Normally, if parents bring a civil lawsuit against your day care, your business liability insurance will cover any litigation costs. However, retaining a criminal defense attorney is different. More likely than not, you will have to pay for your own criminal defense attorney. If you are arrested and cannot afford an attorney, the court can appoint one to you free of charge. If you ask for a court appointed attorney, the court will ask you questions about your income and expenses in order to determine whether you qualify for a free attorney. If you have not been arrested and a welfare agency and/or the police want to talk to you, you are not entitled to a free attorney. (See also our article Finding a Lawyer.)

In conclusion, never lie to a state investigator about what happened to a child. If necessary, consult an attorney who can prepare you for the investigation.

Criminal Investigation

Although a provider is obligated under state child care laws to cooperate with investigators, if law enforcement conducts their own investigation, you have certain rights under the Constitution. Providers must have a general understanding of these rights in case the police decide to question you about a child's injury.

In general, if a police officer wants to talk to you, you are not obligated to speak to him or her. I am not talking about a situation in which you get a traffic ticket and the officer requests basic information, like your name; rather, I am talking about a situation where the police are conducting a formal investigation. By speaking to them, you are voluntarily answering their questions, and what you say can be used against you in a court of law. Many people feel obligated to talk to the police because they believe they may be perceived as having something to hide if they refuse. Again, this is an incorrect assumption.

Be aware that the police do not represent you, nor are they obligated to represent your interests. The police collect facts about the case. If they believe that you have committed a crime, either they or the prosecuting attorney reviewing the case will have you arrested.

If you want to talk to the police, that is a decision that you will have to make.

Some legal misconceptions must be clarified. Many providers believe that the statements they give to the police cannot be used against them if their Miranda Rights—basically, "You have a right to remain silent. Anything that you say can and will be used against you at trial. You have the right to the assistance of an attorney. If you cannot afford an attorney, one will be provided for you free of charge."—were not read to them. Sometimes people assume that the police are always required to read them their Miranda Rights. It is important to know that this is not always true.

Two conditions have to occur for Miranda Rights to be read to you. First, you must not be free to leave the presence of the police, e.g., you are arrested or under their custody. Second, the police must question you about the facts of the underlying case.

Assume that the police come to your house and want to talk to you about a child's injury. Are the police obligated to read you your Miranda Rights? No, because you can tell them you will not speak with them and ask them to leave. You are not under their custody—you are free to go about your business. At that point, the police must leave. You are not required to explain why you do not want to talk to them, even if they ask you why you are unwilling to answer any questions.

What if you decide to speak to the police at your house and you say things that are incriminating, such as telling inconsistent stories about how the child was injured? Can those statements be used against you? Yes. The police did not have to read you your Miranda Rights because you could have told them to leave your home without you making any statement. Again, in order for your Miranda Rights to apply, you have to be questioned by the police and be in a situation where you cannot remove yourself from their presence.

Let's assume that the police ask a provider to come to the police station so that they can find out what happened to the child. Is a provider legally obligated to go to the police station and answer their questions? No. Tell the police that you do not want to come to the police station. You do not have to explain why you refuse to go with them.

What if you do go to the police station but later decide that you don't want to talk to them? Because you voluntarily came to the police station, you can still tell the police that you have changed your mind and do not want to answer any questions. Again, you have the choice to either talk or not talk to the police.

Assume that either the police came to your house and you agreed to speak to them or you went to the police station and agreed to speak to them. What if, after ten minutes of questioning, you no longer want to talk to them? You can stop answering questions at any time. Again, you have the right to refuse to speak with the police. You do not have to tell them anything that can be used against you. Simply say that you do not wish to answer any further questions. Again, you are not obligated to give reasons for your refusal to answer any more questions.

What if you were arrested and you voluntarily made statements that incriminate you? Does the fact that you were arrested require the police to read you your Miranda Rights? No. Even though you are not free to leave because you are under police custody, you spoke voluntarily. The police did not ask you any questions. Any incriminating statements that you made are admissible in a court of law.

The easiest way to stop any police questioning is to tell them that you want to consult an attorney. At that point, any questioning by the police must stop. This is true whether you are free to leave or not, whether the police came to your house or you were brought to the police station.

If the police continue to ask questions, statements you make are not admissible in a court of law. The problem for a provider is that it is difficult to prove that you told the police you wanted to consult with an attorney.

If possible, have a witness with you when you ask for an attorney. Police officers usually have a partner with them so they have a witness to incriminating statements that you make. If the police did not have a partner there to hear what a provider had to say, then it would be a scenario of who said what. Providers must be just as savvy as the police and should have a witness to back up their demand for an attorney so that questioning may stop.

If you decide to go to the police station, the police probably will not allow anyone but you into an interview room. Sometimes they isolate witnesses so that they have an upper hand in the interview. Keep in mind that if you are at home, the police cannot tell you who you can have around during questioning. The police may come to your home when you least expect it and try to catch you off guard. Again, you are under no obligation to talk to them. If they continue to ask you questions, tell them that you want to speak to an attorney.

Even if you do not have a witness available, you can tell the police that you want to consult an attorney. Some police officers, knowing that you do not have a witness to back up your request, will continue to question you in the hopes that you will break down and talk to them. Unethical officers will claim that you did not invoke your right to speak to an attorney.

Another method of handling this situation is to tell them that you are willing to speak to them, but they have to make an appointment for a future date. This will give you an opportunity to find a witness to be with you when they do come to your home. You can then still tell them that you do not want to speak to them and that you want to consult with an attorney. This method should protect you—the police may not be as tempted to keep questioning you. Under no conditions should you sign any documents that the police put before you. You could be signing a confession that you never gave.

When you are invoking your right to have an attorney, you must be clear. The law does not recognize questions like, “Do I need an attorney?” or “Should I call an attorney?” The police are under no obligation to provide you with legal help. Your demand must be clear: “I want to speak to an attorney.”

Even if you do want to speak to the police, I advise that you first consult a criminal defense attorney. Providers often do not understand how their statements can hurt them, even when they believe they are truthful. What providers say is often reviewed by other people, and there is much subjective interpretation of events. Do not assume that others will see the situation as you do. When it comes to injured children, the criminal justice system is more apt to consider you a guilty party. I suggest that you consult with an attorney before you speak to the police. Some people believe that by cooperating with the police they will not face criminal charges. That is a very dangerous and incorrect assumption that may help the police build a better criminal case against you.

If the police want to talk to a child in your day care who is a suspect for hurting another child, use caution, because now you have to deal with both the police and the parents’ reactions. Providers should contact the child’s parents as soon as possible and let them deal with the police. The parents of a suspect child may be upset with a provider if they did not know that the police were questioning him or her. In addition, there may be times when your child is the suspect and the police want to talk to him or her. As the child's provider and legal guardian or parent, you can decline to let the police speak to him or her—as long as the child hasn't been arrested.

Conclusion

Most providers entered the day care profession because they enjoy raising this country's next generation. Like any other business owners, providers face certain risks. It is important that you understand how to handle these risks. This article has tried to outline some areas that I have witnessed that impact a provider's livelihood and possible freedom. Remember, if you are investigated, be honest with the investigator, especially when a child has been accidentally injured. There is no reason to lie. Accidents happen all the time. If necessary, consult an attorney to go over the facts so that you convey the information to a state investigator professionally and with confidence.

If law enforcement becomes involved in the investigation, our Constitution affords us certain rights regarding whether we are required to speak to the police. Again, consult an attorney on this matter. Although there may be costs attached to the representation, you must consider that your years of hard work and reputation within the community you serve could be jeopardized.

Frank Perri has been a criminal defense attorney in Rockford, Illinois, for over ten years. He is also a Certified Public Accountant (CPA), prepares tax returns, and represents providers who are audited by the IRS. He has been assisting day care providers for several years since he observed an increase in the number of criminal investigations of providers.

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At first it may seem like a simple idea.

You want to hire someone to help you in your family child care business for a few hours a week. You want your helper to fill in when you must conduct some personal errands or be away at the dentist. Or you want someone to help you during the summer months.

You know you must treat this person as your employee; not as an independent contractor.

But since you won't be paying your helper much money, how hard can it be to fill out the proper paperwork?

Unfortunately – harder than you think.

Here's a summary of the federal and state payroll tax rules:

Federal

You must obtain an Employer Identification Number (EIN).

You must fill out Form I-9 (Employment Eligibility Verification) to verify that your employee is eligible to work in the U.S. You don't file this form with the IRS; instead keep it in your files.

You must have your employee fill out IRS Form W-4 (Employee's Withholding Allowance Certificate) to determine how much you must withhold in federal income taxes from the employee's pay. You don't file this form with the IRS; instead use it with IRS Publication 15 (Circular E) Employer's Tax Guide to look up how much to withhold.

You must withhold Social Security and Medicare taxes from your employee's paycheck. As an employer you must withhold 7.65% out of the employee's pay. In addition, you must contribute another 7.65% of the employee's pay out of your pocket. For example, if your employee earns $100 in a week, you must withhold $7.65 and pay in another $7.65 (total: $15.30). If you pay less than $4,000 in wages for the year, file the annual IRS Form 944 (Employer's Annual Federal Tax Return). If you pay more than $4,000, file the quarterly IRS Form 941 (Employer's Quarterly Federal Tax Return).

If you pay an employee $1,500 or more in any calendar quarter or had any employee work for you in 20 different weeks during the year, you must pay federal unemployment taxes (FUTA). The tax is 0.6% of your employee's pay and comes out of your pocket. File the annual IRS Form 940 (Employer's Annual Federal Unemployment Tax Return).

At the end of the year you must file IRS Form W-2 (Wage and Tax Statement) that summaries your Social Security and Medicare tax withholding for the year. Give a copy to your employee and send it to the IRS by January 31st.

At the end of the year you must also fill out IRS Form W-3 (Transmittal of Wage and Tax Statements) and send it to the Social Security Administration by March 1st.

If you hire more than one unrelated person, you must pay at least the federal minimum wage of $7.25 per hour (2021). See the Fair Labor Standards Act, Title 29: Labor, Part 552.105. If your state minimum wage is higher, you must pay the state minimum wage. State law may require you to pay the state minimum wage even when hiring only one person.

State

Your state may require you to withhold state income taxes, and pay state unemployment taxes. State laws may also require you to purchase workers' compensation insurance.

State payroll tax laws vary, so check with your state Department of Labor for details.

Ouch! Can all of this really be true?

Yes. These rules apply regardless of how little you pay your employee or how few hours she works for you. You may want to seek help with these forms: talk to a tax professional or a local bookkeeper service.

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